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THE GRAY MARKET AND THE CUSTOMS REGULATION—IS
THE CONTROVERSY REALLY OVER AFTER
K MART CORP. V. CARTIER, INC.?

DONNA M. LACH*

INTRODUCTION

The 1980s have seen an influx of gray market goods into the United States. Gray market goods, while legitimately produced and sold in a foreign country under the authorization of the U.S. trademark owner, enter this country through channels that the U.S. trademark owner has not expressly authorized.¹ These goods are referred to as parallel importations when the U.S. trademark owner is also the importer of the trademarked goods.² Often third parties, who have no association with the business agreement that arranged for the production and distribution of these goods, buy the products abroad, bring them into the United States, and then sell them in the U.S. market in competition with the goods of the owner of the identical U.S. trademark rights.³ Although the goods are genuine in that they bear an authentic, rather than a copied or simulated mark,⁴ they may have been produced for foreign markets⁵ and consequently may be of a quality inferior to that of the product in which the trademark owner has developed a good-will and reputation in the U.S. market. In addition, gray market goods may not carry the same manufacturer warranties.⁶ The influx of gray market goods has generated con-

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1. *Vivitar Corp. v. United States*, 761 F.2d 1552, 1555 (Fed. Cir. 1985), *cert. denied*, 474 U.S. 1055 (1986). "'Authorized' means that the manufacturer has established an exclusive territory or conditions of resale through some contractual agreement or agreements, by which the manufacturer, distributor or trademark registrant generally agrees to sell only to particular entities and not to other entities that may compete with the authorized channel." Staaf, *The Law and Economics of the International Gray Market: Quality Assurance, Free-Riding and Passing Off*, 4 INTELL. PROP. J. 191, 192 (1988).

2. *Vivitar*, 761 F.2d at 1555. This Note will refer to the importation of gray market goods and parallel importation interchangeably.

3. Note, *K Mart Corp. v. Cartier, Inc.: A Black Decision for the Gray Market*. 38 AM. U.L. REV. 463, 465 (1989).

4. *Vivitar*, 761 F.2d at 1555. The importation of copied or simulated marks is forbidden by § 42 of the Lanham Act. See *infra* note 198.

5. Note, *Questioning the Validity of Customs Regulation 133.21: An Analysis of Olympus Corp. v. United States and Coalition to Preserve the Integrity of American Trademarks v. United States*. 24 HOUS. L. REV. 1039, 1041 (1987).

6. Goods bearing a genuine U.S. registered trademark manufactured abroad are sometimes made with different specifications for foreign markets. As a result, the product may not be the same

comitant litigation⁷ that has seen trademark holders and their authorized distributors pitted against retail dealers who have profited from their sales of gray market products.⁸

Congress first addressed the issue of the importation of gray market goods in 1922 when it hurriedly amended the Tariff Act in reaction to the Second Circuit decision in *A. Bourjois & Co. v. Katzel*.⁹ This statute was reenacted later in identical form, becoming section 526 of the Tariff Act of 1930.¹⁰ Section 526(a) prohibits the importation of goods manufactured abroad that bear a trademark owned by a U.S. registered trademark owner without the U.S. trademark owner's consent.¹¹ Opponents of the gray market, who are generally holders of U.S. registered trademarks whose financial interests are being harmed by gray market importations, believe that section 526(a) should be given a literal interpretation and that all gray market goods should be banned. These trademark own-

as the product that is advertised and marketed in the United States. Nolan-Haley, *The Competitive Process and Gray Market Goods*, 5 N.Y.L. SCH. J. INT'L & COMP. L. 231, 234 (1984).

7. Hilliard, *Grey Market Goods: Three Eras of Law*, 25 PAT. L. ANN. § 4.03, at 4-7 (1988). While there were only five reported gray market cases from 1923 to 1982, more than twenty have been reported since 1982. *Id.*

8. Hilke, *Free Trading or Free-Riding: An Examination of the Theories and Available Empirical Evidence on Gray Market Imports*, 32 WORLD COMPETITION 75, 75 (1988).

9. 275 F. 539 (2d Cir. 1921), *rev'd*, 260 U.S. 689 (1923).

10. Section 526 of the Tariff Act has been codified as 19 U.S.C. § 1526. Courts have referred to this statute as either § 526 or as § 1526.

19 U.S.C. § 1526 (1975) reads in relevant part:

(a) Merchandise bearing American Trademark: Importation Prohibited

(a) Except as provided by subsection (d) of this section, it shall be unlawful to import into the United States any merchandise of foreign manufacture if such merchandise, or the label, sign, print, package, wrapper, or receptacle, bears a trademark owned by a citizen of, or by a corporation or association created or organized within, the United States, and registered in the Patent and Trademark Office by a person domiciled in the United States . . . unless written consent of the owner of such trademark is produced at the time of making entry.

(b) Seizure and forfeiture

(b) Any such merchandise imported into the United States in violation of the provisions of this section shall be subject to seizure and forfeiture for violation of the customs laws.

(c) Injunction and damages

(c) Any person dealing in any such merchandise may be enjoined from dealing therein within the United States or may be required to export or destroy such merchandise or to remove or obliterate such trademark and shall be liable for the same damages and profits.

(d) Exemptions

(d)(1) The trademark provisions of this section and section 1124 of Title 15, do not apply to the importation of articles accompanying any person arriving in the United States when such articles are for his personal use and not for sale.

(e) Merchandise bearing counterfeit mark; seizure and forfeiture; disposition of seized goods

(e) Any such merchandise bearing a counterfeit mark . . . imported into the United States in violation of the provisions of section 1124 of Title 15, shall be seized and, in the absence of the written consent of the trademark owner, forfeited for violations of the customs laws.

11. *Id.*

ers, who have made considerable investments in advertising their products and providing warranties, service, and consumer education to the American public, claim that their reputation and sales value are being harmed by the sale of gray market goods.¹² This is because the importers and retailers of gray market goods are able to take advantage of the price differential between U.S. and foreign markets and sell the gray market goods to consumers at considerably lower prices.¹³ Hence, proponents of the gray market importation of goods into this country have favored the interpretation that the Customs Service has given section 526.

The Customs Service, an agency of the Treasury Department, has the responsibility of enforcing and interpreting the Tariff Act.¹⁴ In the Customs regulation, section 133.21(c), the Customs Service has interpreted section 526 to mean that certain imported goods may enter the country even without the express consent of the U.S. trademark owner when the owner of the domestic and foreign trademarks are the same, when they have a parent/subsidiary relationship, or when the U.S. trademark owner has licensed a foreign manufacturer to use the U.S. registered trademark.¹⁵ The recent controversy in the courts regarding the gray market issue has centered on the Customs Service's interpretation of section 526. The circuits were split with two circuits upholding the validity of the Customs regulation and one circuit finding the entire regulation invalid.¹⁶

12. *Vivitar Corp. v. United States*, 761 F.2d 1552, 1556 (Fed. Cir. 1985).

13. *Bender & Gerber, In the Wake of High Court Decision, the Gray Market Gets Grayer*, THE NAT'L L.J., Sept. 19, 1988, at 15, col. 1 (the price differential being the result of different prices being asked for the same goods in different countries—a great disparity between the price charged in the United States and the price charged in a foreign country creates the incentive to engage in the gray market business).

14. 19 U.S.C. § 1624 (1982) reads in relevant part:

General Regulations:

In addition to the specific powers conferred by this chapter the Secretary of the Treasury is authorized to make such rules and regulations as may be necessary to carry out the provisions of this chapter.

15. 19 C.F.R. § 133.21(c) Restrictions not applicable, in relevant part:

The restrictions set forth in paragraphs (a) and (b) of this section do not apply to imported articles when:

(1) Both the foreign and the U.S. trademark or trade name are owned by the same person or business entity;

(2) The foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership or control;

(3) The articles of foreign manufacture bear a recorded trademark or trade name applied under authorization of the U.S. owner.

19 C.F.R. § 133.21(c) (1979).

This regulation also provides an exception to the protection provided to the trademark owner under § 42 of the Lanham Act, which prohibits the importation of goods bearing a trademark that copies or simulates a U.S. registered trademark. For the text of § 42 see *infra* note 198.

16. See *Vivitar Corp. v. United States*, 761 F.2d 1552 (Fed. Cir. 1984), *cert. denied*, 474 U.S. 1055 (1986) (finding the regulations consistent and reasonable and that Congress had implied its

The Supreme Court recently addressed the validity of this controversial Customs regulation vis-à-vis section 526 in *K Mart Corp. v. Cartier, Inc.*¹⁷ All parties with an interest in the fate of the gray market had been waiting for a definitive answer to whether all gray market goods would be banned from entry into the United States. The Supreme Court represented a hope for both sides of the gray market issue. Both proponents and opponents of the gray market were wishing that the Court would espouse the policy that they were advancing. The Court unexpectedly severed a subsection of the regulation, thereby creating a situation in which some gray market goods would be barred entry into the United States and others would continue to be allowed in. The circuit courts as well as the legal scholars had viewed the regulations as a unit and had expected the Court to decide whether gray market goods should or should not be banned entirely.¹⁸ Instead, however, the Court focused on the language of the statute and on whether Customs' interpretation was a permissible construction of the statute.¹⁹ Five Justices upheld the common control exceptions,²⁰ which refer to imported goods if the trademark is owned by the same person or entity or if there is a parent/subsidiary relationship. A different combination of five Justices held invalid the authorized use exception,²¹ which refers to goods produced abroad that bear a registered trademark under the authorization of the U.S. trademark holder.

Policy decisions, however, are not the domain of the Supreme Court. While the Court had the opportunity to decide on a U.S. gray market policy, it based its decision on an analysis of the regulation vis-à-vis the words of the statute written over sixty years ago. The result was justifiable as a linguistic study but arbitrary as a gray market policy in that Customs will now have to bar the entry of some but not all gray market goods. An analysis of the *K Mart* decision and the procedural

consent to the regulation); *Olympus Corp. v. United States*, 792 F.2d 315 (2d Cir. 1986), *cert. denied*, 108 S. Ct. 2033 (1988) (upholding the regulations on the grounds of congressional acquiescence and a longstanding interpretation of § 526 by the Customs Service); *Coalition to Preserve the Integrity of American Trademarks v. United States*, 790 F.2d 903 (D.C. Cir. 1986), *rev'd in part and aff'd in part sub nom.*, *K Mart Corp. v. Cartier, Inc.*, 108 S. Ct. 1811 (1988) (finding the regulations invalid because the language of § 526 is unambiguous and the legislative history of § 526 showed that the interpretation of the statute by the Customs Service was not a reasonable one); *United States v. Eighty-Nine Bottles of Eau de Joy*, 797 F.2d 767, 770 (9th Cir. 1986) (though not directly addressing the issue of the validity of the regulations, finding that the legislative intent in passing § 526 of the Tariff Act was "to bar the importation of genuine goods unless authorized by the domestic trademark holder"). See also *infra* notes 176-197 and accompanying discussion.

17. 108 S. Ct. 1811 (1988).

18. Hilke, *supra* note 8, at 75.

19. *K Mart*, 108 S. Ct. at 1817.

20. § 133.21(c)(1) & (2).

21. § 133.21(c)(3).

history that led up to it demonstrates the shortcomings of the Supreme Court in a policy-making capacity.

This Note will focus on the Supreme Court's decision in *K Mart* and the Court's inability to resolve issues that are essentially policy questions. Part I will discuss the pros and cons of the gray market in general, while Part II will address the different interpretations of legislative history that influenced the Justices and the courts to draw their divergent conclusions. After an examination of the history of the *K Mart* case, Part III will analyze the reasoning in the three opinions. Then, Part IV will consider the impact of the decision on the gray market. This Note will discuss the policy considerations that can be resolved by only Congress, concluding that Congress should decide on an overall gray market position that would include a reassessment and clarification of the extent of protection provided by section 526 of the Tariff Act of 1930. Finally, this Note will recommend a ban on all gray market importations.

I. THE GRAY MARKET CONTROVERSY

The business of parallel importation involves goods that are generally well-known brands of high quality²² and has an estimated value of nearly \$10 billion a year.²³ The gray market importation of goods flourished in the early 1980s as a result of the U.S. dollar's dramatic appreciation on the international exchange.²⁴ The scenario in which the gray market "problem" arises is an international business arrangement in which a good bearing a registered U.S. trademark is produced abroad under the authorization of the U.S. trademark holder. Typically this arrangement can be either one in which the U.S. trademark owner is also the owner of the foreign company or one in which the trademark owner sets up a parent/subsidiary or a licensing relationship with a foreign manufacturer to produce the goods. The business arrangement can also be one in which a foreign business sets up a U.S. distributor or subsidiary that registers the foreign trademark in the U.S. The arrangement inevitably involves restrictions imposed by the business agreement for importation of the goods into the U.S. through certain designated distribution

22. Staaf, *supra* note 1, at 193-94. For example, the organization, COPIAT, has among its members the holders of well-known, high quality trademarks, such as Cartier and Charles of the Ritz. The goods come from approximately twenty different countries. *Id.* at 194.

23. Kersner & Stein, *Judicial Construction of Section 526 and the Importation of Grey Market Goods: From Total Exclusion to Unimpeded Entry*, 11 N.C.J. INT'L. L. & COM. REG. 251, 251 (1986). See also Note, *Grey Market Imports: A Genuine Problem for the United States Trademark Owner. Customs Service, and Courts*, 7 NW. J. INT'L. L. & BUS. 762, 762 n.1 (1986).

24. "A commercial fact of life is that the gray market is very much a creature of the fluctuating dollar." Bender & Gerber, *supra* note 13, at 15, col. 1.

channels. The gray market "problem" then arises when the business arrangements are frustrated, usually by third parties unrelated to the agreement, who purchase the goods abroad and then import them for sale in the United States.

The conflict exists between those importers and retailers who profit from the sale of gray market goods in this country and the holders of U.S. registered trademarks who contend that their legally protected property rights have been violated. The legal question in the controversy comes down to whether U.S. trademark protection requires Customs to stop the entry of the gray market goods at the border. Customs regulation section 133.21(c) has had the effect of letting third parties bring in goods that bear a U.S. registered trademark without the permission of the trademark holder.²⁵ The broader policy question, however, concerns a conflict of values between the importance of permitting free competition in the American market and the need for protecting the property rights of the trademark holder.²⁶

The competing arguments can be delineated as follows. Trademark owners emphasize that a trademark protects their interests and that the gray market importation of goods contravenes that protection. The trademark, "a monopoly conferred by law,"²⁷ protects its holder in several ways. It symbolizes the goodwill and reputation that the trademark owner has established in the product. It also distinguishes the trademark owner's goods from other goods by signifying a single source of production and level of quality. Finally, it represents the trademark holder's investment in this quality and in advertising and customer service.²⁸ These opponents of the gray market note a number of reasons why gray market sellers can sell goods at lower prices: the fluctuations in international currency markets, lower labor and materials costs in different countries, arbitrary price discrimination,²⁹ and also the fact that the gray

25. *Olympus Corp. v. United States*, 792 F.2d 315, 317 (2d Cir. 1986). Customs maintains that a trademark owner cannot infringe its own mark, which is why it treats the U.S. company and the foreign company "as being constructively one for infringement purposes." *Lever Bros. v. United States*, 877 F.2d 101 (D.C. Cir. 1989).

26. Comment, *Preventing the Importation and Sale of Genuine Goods Bearing American-Owned Trademarks: Protecting an American Goodwill*, 35 ME. L. REV. 314, 338 (1983).

27. *Osawa & Co. v. B & H Photo*, 589 F. Supp. 1163, 1176 (S.D.N.Y. 1984). See also Mackintosh, with editorial contributions by Graham, *Grey Market Imports: Burgeoning Crisis or Emerging Policy*, 11 N.C.J. INT'L. L. & COM. REG. 293, 296-97 (1986) (like patents and copyrights, trademarks are limited monopolies, with the exception that patent and copyright rights are created by statute, whereas trademark rights come from prior use in trade).

28. Note, *Trademark Law, Economics and Grey-Market Policy*, 62 IND. L.J. 753, 755 (1987). The trademark helps consumers to identify products that they wish to purchase again, and the "tendency to make repeat purchases . . . is the basis of the producer's goodwill." *Id.*

29. Price discrimination is the result of firms charging different prices in different locations.

market seller does not have the expenses involved with advertising, consumer education, or warranty and service that the trademark holder has.³⁰

Those opposed to the gray market importation of goods into the United States contend that gray market goods mislead consumers and that gray market importers get a free-ride on the promotional efforts of the trademark owner.³¹ First, since gray market goods are marketed outside the trademark owner's authorized channels of distribution that are responsible for the promotion, support, and service of the product in the United States,³² most gray market sellers rely on the reputation that the trademark owner has established in order to create a demand for their products. As a result, gray market sellers have no incentive to maintain a product quality as high as that of the trademark owner.³³ Thus, gray market opponents claim that consumers are misled because they expect the same warranty and products liability protection and warranty service, as well as other protections such as quality and safety, offered by the U.S. trademark holder.³⁴ The differences in such protections offered by gray market goods lead to consumer confusion as to the source and quality of goods.³⁵ Secondly, opponents argue a related point that gray market importers free-ride on the goodwill and reputation that the U.S. trademark holder has developed, resulting in a loss of time, energy and money for the registered trademark holder. The gray market importer takes advantage of the advertising of the trademark holder, while the trademark holder's sales might actually decline because of the confusion caused by the differing prices and quality.³⁶ Finally, opponents point out that the continued influx of gray market goods may eventually

Gray marketers profit from price discrimination by buying goods in a market in which the goods are sold at a lower price than they are sold in their U.S. market and then reselling them in the United States. Hilke, *supra* note 8, at 78-79.

30. *Osawa*, 589 F. Supp. at 1176.

31. Fitzpatrick & Brunet, *Barring Importation of Gray Goods Under Section 42 of The Lanham Act, and Section 526 of the Tariff Act*, in *GRAY MARKETS AND PARALLEL IMPORTATION* 9, 12 (Practising Law Institute ed. 1986).

32. *COPIAT v. United States*, 598 F. Supp. 844, 850 (D.D.C. 1984).

33. Note, *Vivitar Corp. v. United States: Protection Against Gray Market Goods Under 19 U.S.C. Section 1526*, 60 S. CAL. L. REV. 179, 194 (1986) (the exception to this rule being some large gray market sellers such as K-Mart, which offers its own service and warranties on gray market goods).

34. Fitzpatrick & Brunet, *supra* note 31, at 11-12.

35. "Source" includes not only the geographic origin of the goods, but also the entire chain of distribution upon which the consumer can rely. "Quality" includes the trademark owner's investment not only in the consistency in the product, but also in inventory and quality controls, shipping, and storage. See generally, Note, *The Gray Market Case: Trademark Rights v. Consumer Interests*, 61 NOTRE DAME L. REV. 838, 855-56 (1986).

36. Note, *supra* note 33, at 198-99. Free-riders benefit from the trademark holder's investments in advertising, warranties, dealer training, quality inspection and repair service, while consumers

lead to unemployment in the domestic industry, which will affect the consumers' interests in the long run.³⁷

Proponents of the gray market, on the other hand, contend that the gray market importation of goods protects consumer interests by promoting competition and maintaining low prices.³⁸ In this vein, they argue that the trademark protection of section 526 of the Tariff Act of 1930 encourages anti-competitive practices and violations of antitrust law and policy.³⁹ This is true, they argue, because foreign businesses set up subsidiaries or licensees in the United States to register their trademarks and then charge inflated prices for their trademarked goods in their American market. The result is that American consumers pay significantly higher prices than their foreign counterparts for the same goods.⁴⁰ The proponents also note that recently many of the larger retail dealers of gray market goods have begun providing their own warranties and other services that cover these goods,⁴¹ thereby weakening the opponents' argument of consumer confusion.

The theory of trademark exhaustion is used to justify the importation of gray market goods. Under this theory, once the first sale of a marked good takes place after the good has entered the stream of commerce in the trademark owner's territory, the trademark owner's rights are "exhausted," that is to say, the trademark owner can no longer control sales of the trademarked goods.⁴² It has also been argued that the trademark owner also loses rights to control subsequent sales of trademarked goods even once the goods have been sold abroad.⁴³ Courts that have considered the exhaustion theory are split in applying it to situations in which the U.S. trademark holder had established a separate and distinct goodwill in its product. One court conceded that an assignee of the trademark in a second country can, in fact, develop a "separate, fac-

become confused when they buy products of a lesser quality than represented by advertising, which results in an eventual decline in purchases of the trademark owner's product. *Id.*

37. Nolan-Haley, *supra* note 6, at 233.

38. Note, *supra* note 35, at 839.

39. Osawa & Co. v. B & H Photo, 589 F. Supp. 1163, 1176 (S.D.N.Y. 1984) (where defendants argued that § 526 encourages discriminatory pricing by allowing higher prices to be charged to U.S. distributors, which, in turn, means that the U.S. consumer pays the higher, discriminatory price). The scope of this Note does not reach the antitrust issue.

40. Kelly, *An Overview of the Influx of Grey Market Goods Into the United States*, 11 N.C.J. INT'L. L. & COM. REG. 231, 250 (1986).

41. Hilke, *supra* note 8, at 89 (for example, K-Mart and Wards).

42. Note, *supra* note 35, at 853. The exhaustion theory, however, does not make clear why trademark rights should be exhausted after marketing the trademarked goods. Takematsa, *Parallel Importation of Trademarked Goods: A Comparative Analysis*, 57 WASH. L. REV. 433, 456-57 (1982).

43. Note, *The Greying of American Trademarks: The Genuine Goods Exclusion Act and the Incongruity of Customs Regulation* 19 C.F.R. § 133.21, 54 FORDHAM L. REV. 83, 109 (1985).

tually independent goodwill,"⁴⁴ holding that the trademark holder was entitled under both section 526 and trademark infringement to the injunctive relief sought. Similarly, where the plaintiff had provided a toll-free number plus consumer education, the court found that even when an assignment is revocable, it is possible to establish a separate, factually distinct goodwill in the assigned trademark.⁴⁵ That court enjoined the importation of the gray market products because it infringed on the trademark holder's rights under both section 526 and the Lanham Act.⁴⁶ Conversely, another court found no basis for protecting a trademark holder's domestic goodwill where the U.S. trademark holder is "a cog or entity" in a single international conglomerate.⁴⁷ The Ninth Circuit refused to enjoin the importation of gray market computer chips where a U.S. wholly-owned subsidiary had been assigned the trademark rights of the Japanese parent.⁴⁸ The court reasoned that the U.S. trademark laws do not offer foreign companies "a vehicle for establishing a worldwide discriminatory pricing scheme simply through the expedient of setting up an American subsidiary with nominal title to its mark."⁴⁹

The parallel importation of trademarked goods is not unique to the United States. Many of our trading partners have authorized the parallel importation of goods in their courts or through treaties or legislation.⁵⁰ The courts of other nations have considered various theories in their analyses of gray market importations. For example, one German court, invoking the theory of exhaustion of trademark rights, held that a trademark owner loses control of the trademarked goods once the goods are put on the market in no matter which country.⁵¹ Another German court held that since the function of a trademark is to indicate the commercial source of origin, even if the goods differed in quality, the parallel importation by third parties did not infringe the trademark rights.⁵² A Cana-

44. *Osawa & Co. v. B & H Photo*, 589 F. Supp. 1163, 1174 (S.D.N.Y. 1984). Moreover, the court questioned the soundness of "these crude regulations," meaning § 133.21(c). *Id.* at 1178.

45. *Premier Dental Prods. Co. v. Darby Dental Supply Co.*, No. 85-1780, slip op. (E.D. Pa. July 16, 1985), *aff'd*, 794 F.2d 850 (3d Cir. 1986), *cert. denied*, 479 U.S. 950 (1986), *reh'g denied*, 479 U.S. 1062 (1987).

46. *Id.*

47. *Parfums Stern, Inc. v. United States Customs Ser.*, 575 F. Supp. 416, 418 (S.D.Fl. 1983). The court further noted that the defendants had relied on the plaintiff's acquiescence to their practice of importing gray market goods and that the public benefited from the lower prices. *Id.* at 420.

48. *NEC Electronics v. Cal Circuit Abco*, 810 F.2d 1506 (9th Cir. 1987).

49. *Id.* at 1511. The court stated that the trademark law is designed to prevent consumer confusion, which does not exist with a genuinely trademarked article. *Id.* at 1509.

50. *Gorelick & Little, The Case for Parallel Importation*, 11 N.C.J. INT'L L. & COM. REG. 205, 227 (1986). Parallel importation is permitted in most "economically significant" countries. *Id.*

51. *Takamatsu*, *supra* note 42, at 445, discussing *Maja*, Judgment of Jan. 22, 1964, Fed. Sup. Ct. (W. Ger.).

52. *Id.*, discussing *Cinzano & Co. GmbH v. Java Kaffeegeschfte GmbH & Co.*, Judgment of

dian court refused to invoke either the doctrine of "passing off"⁵³ or a claim of unfair competition to prevent parallel importation where there was no evidence of deception or consumer confusion,⁵⁴ especially since the court found that such a prohibition would result in a monopoly situation in which only an authorized dealer could sell a "complete package."⁵⁵ The factors that one Japanese court considered in facing the question of parallel importation were whether: 1) the trademark indicated the manufacturer or the local distributor as the source of the goods; 2) the goods were of equal quality; 3) the exclusive distributor's goodwill was based on the brand name's reputation in the world market; 4) the parallel importation would promote free and fair competition in both price and service; and 5) the importer of gray market goods was taking advantage of the distributor's advertising.⁵⁶

In addition, some nations have entered into treaties or passed legislation that make provisions for parallel importations. For example, in the European Economic Community, the Treaty of Rome, which views any export restriction as inherently anti-competitive and thus a *per se* violation of the Treaty, takes precedence over the domestic law of the member nations.⁵⁷ As a result, in a country like France, an authorized seller can sue a parallel seller for unfair competition, but the trademark holder cannot prevent the importation of such goods.⁵⁸ Japan has passed legislation that provides that gray market goods will not be excluded from the country where 1) the domestic trademark holder also holds the foreign trademark and is supplying the goods to the third party; and 2) the domestic and foreign trademark holders are part of the same business entity.⁵⁹ Finally, the United Nations Conference on Trade and Develop-

Feb. 2, 1973, Fed. Sup. Ct. (W. Ger.). Similarly, an Austrian court relied on the exhaustion theory and the functions of the trademark to deny injunctive relief against parallel importation. *Id.* at 446, discussing *Agfa-Gevaert GmbH v. Schark*, Judgment of Nov. 30, 1970, Sup. Ct. (Aus.).

53. Staaf, *supra* note 1, at 206. "Passing off" emphasizes consumer deception or confusion. *Id.*

54. *Id.* at 197.

55. Kelly, *supra* note 40, at 238, discussing *Consumers Distributing Co. Ltd. v. Seiko Time Canada Ltd.*, [1984] 1 S.C.R. 583.

56. Takamatsu, *supra* note 42, at 442, discussing *Nestle Nihon K.K. v. Sankai Shoten* (unreported case, Tokyo Dist. Ct., May 29, 1965). In Japan, where there was a substantial difference in taste between the domestic distributed coffee and the gray market coffee, the court found that consumers may be deceived by the difference in quality and enjoined the parallel importation. *Id.* at 440. But where there was no difference in quality, the Japanese court rejected the principle of territoriality (*see infra* notes 105-106 and accompanying discussion.) and instead focused on the function of the trademark, applying the criminal law theory of "illegal in substance." Since there was nothing "illegal in substance" in the lawsuit, the court permitted the parallel importation. *Id.* at 442.

57. Staaf, *supra* note 1, at 198 (the European Court of Justice views all vertical restraints within the EEC *per se* illegal).

58. *Id.* at 199.

59. Takamatsu, *supra* note 42, at 443. Japan amended its Customs Duties Act in 1972 to allow

ment has stated that enterprises should refrain from restricting the parallel importation of goods where the only purpose of such a restriction would be to maintain artificially high prices.⁶⁰

There have been several attempts to confront the gray market issue in this country by various levels of government. In an effort to formulate a comprehensive U.S. policy regarding the gray market, the Reagan Administration appointed a committee composed of representatives from various agencies.⁶¹ The committee only was able to present to the Cabinet Council on Commerce and Trade a list of policy options rather than a definitive solution. Its options were: 1) maintain the status quo where foreign and U.S. trademark owners are related; 2) impose a mandatory labeling system to inform consumers that the goods are not subject to the same warranty and service benefits as U.S. goods; 3) amend section 337 of the Tariff Act of 1930 to facilitate gray market challenges in court; 4) maintain the status quo where gray market goods are identical to the U.S. trademark counterparts; 5) require the removal or obliteration of the infringing trademark on the gray market goods; and 6) prohibit the importation of all gray market goods that do not have the U.S. trademark owner's written consent.⁶²

The Customs Service also attempted to resolve the gray market problem when it solicited public comment on the issue of parallel importation. Specifically, the solicitations concerned two alternative approaches to the gray market problem: mandatory labeling and mandatory removal of the trademark.⁶³ In the meanwhile, however, the Supreme Court agreed to hear *K Mart*, and the Customs Service did not move forward on either of these approaches.⁶⁴

States have addressed the gray market problem, especially in the area of consumer protection. For example, to cope with the consumer confusion created by gray market goods, a few states have enacted statutes requiring retailers to post notices indicating that certain gray market goods may not carry the same warranties as other goods with the same brand name and also that the goods might not have instructions in the

parallel importation under certain circumstances. The amendment represented a significant change from its previous position. *Id.*

60. Gorelick & Little, *supra* note 50, at 228, citing Principle D4 of *The Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices*. U.N. Conference on Trade and Development at 10-11, U.N. Doc. TD/RBP/CONF/10/Rev.1 (1980).

61. Mackintosh, *supra* note 27, at 293 n.3. The agencies involved were the Departments of State, Commerce and Treasury, the Office of Management and Budget, the Council of Economic Advisors, the U.S. Trade Representatives Office, and the Justice Department. *Id.*

62. *Id.* at 293 n.4.

63. 51 Fed. Reg. 22005 (1986).

64. Hilke, *supra* note 8, at 75-76 n.4.

English language.⁶⁵

At the congressional level, Senator Chafee unsuccessfully introduced a bill to the Senate Committee on Finance in 1986 that would have amended both section 526 of the Tariff Act and section 42 of the Lanham Act to allow the importation of gray market goods.⁶⁶ Since the *K Mart* decision, two bills have been introduced that would have an impact on

65. California, New York, and Connecticut have passed such statutes. The California statute reaches all retailers who sell gray market goods, whereas the New York and Connecticut statutes only reach retailers who "knowingly" sell such goods.

The California law provides in relevant part:

(a) Every retail seller who offers grey market goods for sale shall post a conspicuous sign at the product's point of display and affix to the product or its package a conspicuous ticket, label, or tag disclosing any or all of the following, whichever is applicable:

- (1) The item is not covered by a manufacturer's express written warranty valid in the United States (however, any implied warranty provided by law still exists).
- (2) The item is not compatible with United States electrical currents.
- (3) The item is not compatible with United States broadcast frequencies.
- (4) Replacement parts are not available through the manufacturer's United States distributors.
- (5) Compatible accessories are not available through the manufacturer's United States distributors.
- (6) The item is not accompanied by instructions in English.
- (7) The item is not eligible for a manufacturer's rebate.
- (8) Any other incompatibility or nonconformity with relevant domestic standards known to the seller.

CAL. CIV. CODE § 1797.81 (West 1988).

The New York statute provides in relevant part:

2. Every retail dealer who knowingly offers for sale grey market merchandise shall conspicuously post, in the following manner, the information required by subdivision three of this section:

- a. On a sign attached to the item itself; or
- b. On a sign affixed to each cash register or point of sale at which such goods are offered for sale; or
- c. On a sign so situated as to be clearly visible to the buyer from the register.

3. Every retail dealer who offers for sale grey market merchandise shall disclose, as applicable, that either some of the products or a specific product are not:

- a. accompanied by the manufacturer's warranty valid in the United States; or
- b. accompanied by instructions in English; or
- c. eligible for a rebate offered by the manufacturer.

N.Y. GEN. BUS. LAW § 218-aa (McKinney 1988).

The Connecticut statute provides in relevant part:

(b) Every retail dealer who knowingly sells or offers for sale any gray markets merchandise shall post conspicuously, on a sign attached to the item itself, on a sign affixed to each cash register or point of sale at which such goods are offered for sale, or on a sign so situated as to be clearly visible to the buyer from the register, that either some of the products or a specific product are not: (1) Accompanied by the manufacturer's warranty valid in the United States; (2) accompanied by instructions in English; or (3) eligible for a rebate offered by the manufacturer.

(c) Every retail dealer or dealer engaged in a mail-order business who offers for sale gray markets merchandise shall include the disclosure required by subsection (b) of this section in any written advertisement relating to such product. Such disclosure shall be made in type of a conspicuous size.

CONN. GEN. STAT. § 42-210 (West 1986).

66. Senator Chafee's bill reads:

To provide for parallel imports in order to continue to provide savings for United States consumers.

Be it enacted by the Senate and House of Representatives of the United States of

the protection offered by section 526 and on the gray market in general.⁶⁷ Representative Chandler has introduced a bill to amend the Tariff Act to permit parallel importation and codify the Customs regulation, section 133.21(c), thereby overturning *K Mart's* invalidation of Customs' authorized use exception.⁶⁸ Senator Hatch has introduced a bill to amend the

America in Congress assembled. That this Act may be cited as the "Price Competitive Products Act of 1986."

SEC. 2. Section 526 of the Tariff Act of 1930 is amended by adding at the end thereof the following:

"(f)(1) Nothing in this section shall restrict the importation or sale of foreign-made articles bearing a trademark or trade name identical with one owned and registered by a citizen of the United States or a corporation or association created or organized within the United States when—

"(A) both the foreign and the United States trademark or trade name are owned by the same person or business entity;

"(B) the foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership and control; or

"(C) the articles of foreign manufacture bear a recorded trademark or trade name applied under authorization of the United States owner.

"(2) As used in paragraph (1), the term—

"(A) 'common ownership' means individual or aggregate ownership of more than 50 percent of the business entity; and

"(B) 'common control' means effective control in policy and operations and is not necessarily synonymous with common ownership."

SEC. 3. Section 42 of the Act of July 5, 1949 (15 U.S.C. 1124), known as the Lanham Trademark Act, is amended by—

(1) inserting "(a)" before "Except"; and

(2) adding at the end thereof the following:

"(b)(1) Nothing in this section shall restrict the importation or sale of foreign-made articles bearing a trademark or trade name identical with one owned and registered by a citizen of the United States or a corporation or association created or organized within the United States when—

"(A) both the foreign and the United States trademark or trade name are owned by the same person or business entity;

"(B) the foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership or control; or

"(C) the articles of foreign manufacture bear a recorded trademark or trade name applied under authorization of the United States owner.

"(2) As used in paragraph (1), the term—

"(A) 'common ownership' means individual or aggregate ownership of more than 50 percent of the business entity; and

"(B) 'common control' means effective control in policy and operations and is not necessarily synonymous with common ownership."

S. 2614, 99th Cong., 2d Sess. (1986).

67. At the time of publication of this Note, both bills are pending in Congress.

68. H.R. 771, 101st Cong., 1st Sess. (1989). The House bill, introduced by Representative Chandler on February 2, 1989, would validate the entry of gray market goods by amending the Tariff Act. This bill would codify the Customs regulation, including the "authorized use" exception invalidated by *K Mart*. *Bill is Introduced in House to Codify Customs Position on Gray Market Imports*, 6 INT'L. TRADE REP. (BNA) 7, at 200 (Feb. 15, 1989).

The bill reads:

To provide for the continuation of parallel imports under section 526 of the Tariff Act of 1930.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Price Competitive Products Act of 1989."

Sec. 2. Section 526 of the Tariff Act of 1930 (19 U.S.C. 1526) is amended by adding at the end thereof the following:

Lanham Act that would prohibit all gray market importations, which includes the scope of section 526 and invalidates the exclusionary Customs regulation.⁶⁹ Thus, both new bills aim to overturn the *K Mart*

"(f)(1) Nothing in this Act or the Act of July 5, 1946 (60 Stat. 427; chapter 540) shall restrict the importation or sale of foreign-made articles bearing a trademark or trade name identical with one owned and registered by a citizen of the United States or a corporation or association created or organized within the United States if—

"(A) both the foreign and the United States trademark or trade name are owned by the same person or business entity;

"(B) the foreign and domestic trademark or trade name owners are parent and subsidiary companies or are otherwise subject to common ownership or control; or

"(C) the articles of foreign manufacture bear a recorded trademark or trade name applied under authority of the United States owner.

"(2) For purposes of this subsection—

"(A) The term 'common ownership' means individual or aggregate ownership of more than 50 percent of the business entity.

"(B) The term 'common control' means effective control in policy and operations and is not necessarily synonymous with common ownership.

"(3) Notwithstanding any provision of title 17, United States Code, the importation or sale of any article that could otherwise be legally imported shall not be restricted by reason of a copyright in its trademark or in the label, package, design, instructions for use, or other material accompanying the article."

69. S. 626, 101st Cong., 1st Sess. (1989). The Senate bill, introduced by Senator Hatch on March 16, 1989, would ban all gray market goods, whether or not they copy or simulate a U.S. registered trademark, by amending the Lanham Act. This bill would invalidate all of the exceptions to trademark protection under both the Lanham Act and the Tariff Act that Customs has created in § 133.21(c).

The bill reads:

To amend the Lanham Trademark Act regarding gray market goods.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Trademark Protection Act of 1989."

(b) The Congress finds that —

(1) the importation and/or sale of gray market goods (which are, for purposes of this Act, goods manufactured abroad to which a foreign trademark is lawfully applied but which are imported into the United States without the authorization of the United States owner of the identical or similar trademark), fundamentally violate United States trademark law;

(2) gray market goods cause confusion to consumers that trademark laws are designed to avoid because such goods, intended for sale abroad, frequently differ in their physical characteristics from goods intended for sale in the United States, such as—

(A) gray market cosmetics may contain ingredients that are either banned in the United States or are otherwise considered less desirable from the perspective of a United States consumer;

(B) gray market vehicles may not include safety devices common in vehicles manufactured for sale in the United States market;

(C) gray market batteries may have shorter lives when sold to a United States consumer simply because of delays and lack of care in trans-shipment; and

(D) gray market goods are frequently not subject to the same quality control, warranties provided in the United States and other features that consumers may expect from a particular trademarked good;

(3) whether or not consumers are confused by gray market goods, the importation or sale of such goods deprives United States trademark owners of their investment in their trademark;

(4) trademarks foster vigorous competition and increased research and de-

result.

Former President Reagan had an opportunity to voice his opinion on policy regarding the gray market issue when, pursuant to his power under section 337(g)(2)⁷⁰ of the Tariff Act of 1930, he disapproved of the

velopment and such interbrand competition ultimately benefits consumers with lower prices and increased quality and selection;

(5) the loss of goodwill occasioned by gray market goods is in violation of fundamental tenets of our trademark laws; and

(6) the importation and sale of gray market goods in the United States must be prevented to preserve the integrity of our trademark system.

(c) The Act of July 5, 1946, the Lanham Trademark Act (15 U.S.C. 1051 et seq.), is amended by adding at the end thereof the following new section:

"Sec. 52.(a) No person may import into or sell within the United States any good that is manufactured outside the United States if such good, or the label, sign, print, package, wrapper, or receptacle, bears a trademark that is identical to a trademark—

"(1) owned by a person that is a citizen of the United States or by a corporation or other entity created within the United States under the laws thereof or the laws of one of the States, the District of Columbia, one of the territories, or the Commonwealth of Puerto Rico, without regard to the citizenship of its incorporators, shareholders, officers, or directors, and

"(2) registered by such person with the Patent and Trademark Office under the provisions of this Act, unless such person consents to such importation or sale.

"(b) The prohibitions of subsection (a) apply regardless—

"(1) of whether the foreign manufacturer of the goods or foreign trademark owner whose trademark appears on the goods is related in any way, by corporate affiliation or otherwise, to the owner of the United States trademark;

"(2) of whether the owner of the United States trademark owns or has registered the trademark abroad; or

"(3) of whether the owner of the United States trademark has authorized the use of the trademark abroad.

"(c) The Secretary of the Treasury shall exclude from entry into the United States any good the importation of which is in violation of subsection (a), provided that the person who owns the trademark in question in the United States and who has registered that trademark with the Patent and Trademark Office files a copy of the certificate of registration for such trademark with the Secretary of the Treasury.

"(d) Any owner of a United States trademark may bring an action against the importer or seller of goods that bear identical trademarks in violation of section (a) in any Federal district court to enjoin such importation or sale and to obtain money damages and lost profits for the wrongful use of a trademark by reason of such importation or sale, under the provisions of this Act.

"(e) For purposes of this section, the term—

"(1) 'person' means any individual or entity including but not limited to any corporation or partnership; and

"(2) 'United States' means the territory comprising the 50 States, the District of Columbia, and Puerto Rico.

"(f) The exceptions to the prohibitions of section 526(a) of the Tariff Act of 1930, set forth in section 526(d) of that Act, apply to the prohibitions set forth herein.

"(g) The Secretary may promulgate regulations to implement subsection (b) but such regulations must enforce subsection (b) fully for any owner of a trademark in the United States regardless of whether—

"(1) such trademark owner or its subsidiary or other affiliate manufactures or sells goods bearing an identical or similar trademark abroad;

"(2) such trademark owner owns and/or has registered such trademark abroad; or

"(3) such trademark owner has authorized the use of such trademark abroad."

70. 19 U.S.C. § 1337(g)(2) (1982):

determination of the International Trade Commission in *In re Certain Alkaline Batteries*.⁷¹ *Alkaline Batteries*, more commonly referred to as the Duracell Case, was brought as a violation of section 337⁷² of the Tariff Act of 1930, alleging that plaintiff's sale of batteries was being undercut by the unauthorized importation of genuine Duracell batteries from Belgium that were manufactured there for European consumption.⁷³ The United States International Trade Commission held that the importation of the gray market batteries constituted a trademark infringement.⁷⁴ The Commission added that the "origin" of a product is not just the "manufacturer but also the distribution chain."⁷⁵ While section 526 was not challenged in this case, Vice Chairman Liebler added an opinion in which he disagreed that section 526 was intended to only cover a situation in which a U.S. company buys the trademark rights of a foreign company.⁷⁶ President Reagan stated that the International Trade Commission's interpretation of section 42 of the Lanham Act was "at odds with the longstanding regulatory interpretation by the Department of the Treasury . . . [and with] [r]ecent decisions that explicitly uphold the Treasury Department's interpretation."⁷⁷ In effect, the President was

(2) If, before the close of the 60-day period beginning on the day after the day on which he receives a copy of such determination, the President, for policy reasons, disapproves such determination and notifies the Commission of his disapproval, then, effective on the date of such notice, such determination and the action taken under subsection (d), (e), or (f) of this section with respect thereto shall have no force or effect.

71. 6 I.T.R.D. 1864 (1984).

72. 19 U.S.C. § 1337 (1975). Unfair practices in import trade. § 337(a) reads:

(a) Unfair methods of competition and unfair acts in the importation of articles into the United States, or in their sale by the owner, importer, consignee, or agent of either, the effect or tendency of which is to destroy or substantially injure an industry, efficiently and economically operated, in the United States, or to prevent the establishment of such an industry, or to restrain or monopolize trade and commerce in the United States, are declared unlawful, and when found by the Commission to exist shall be dealt with, in addition to any other provisions of law, as provided in this section.

73. *Alkaline Batteries*, 6 I.T.R.D. at 1851.

74. *Id.* at 1852. Violations of § 337 were found on six grounds:

1) infringement of a registered trademark under the common law of trademarks; 2) violation of § 42 of the Lanham Act; 3) violation of § 32(1) of the Lanham Act; 4) misappropriation of trade dress; 5) false designation of origin; and 6) violations of the Fair Packaging and Labeling Act.

75. *Id.* at 1864 (holding that defendants violated § 337 because they had violated § 43(a) of the Lanham Act, which controls the false designation of origin).

76. "Just because section 526 was enacted in response to the decision of the Court of Appeals in *Bourjois* does not imply that the statute should only control the narrowest version of the facts presented in *Bourjois*." *Id.* at 1869.

77. Note, *Parallel Importation—Legitimate Goods or Trademark Infringement?* 18 VAND. J. TRANSNAT'L. L. 543, 571(1985), citing Letter from President Ronald Reagan to Paula Stern, Chairman, United States International Trade Commission (Jan. 4, 1985):

The Commission's interpretation of section 42 of the Lanham Act (15 U.S.C. 1124), one of several grounds for the Commission's determination, is at odds with the longstanding regulatory interpretation by the Department of the Treasury. . . . The Administration has advanced the Treasury Department's interpretation in a number of pending court cases. Recent decisions explicitly uphold the Treasury Department's interpretation. Al-

referring to *Vivitar*⁷⁸ and the District Court decision in *COPIAT*,⁷⁹ which upheld the validity of the Customs regulation. Since the time the President wrote this letter, *COPIAT* was reversed by the Circuit Court of the District of Columbia, which, in turn, was affirmed in part and reversed in part in *K Mart*.

II. THE LEGAL FRAMEWORK

A. Section 526 of the Tariff Act of 1930

The legal issue in the gray market controversy has centered on the interpretation of the extent to which section 526 of the Tariff Act of 1930 protects trademark holders. A discussion of the legislative history of section 526 necessarily begins with the Second Circuit decision in *A. Bourjois & Co. v. Katzel*,⁸⁰ to which Congress reacted, at least in part, with the enactment of section 526 while the case was still pending in the Supreme Court. In *Katzel, A. Bourjois & Co.*, an American firm, purchased all of the U.S. business and goodwill of a French producer's business in "Java" face powder.⁸¹ A. Bourjois & Co., having paid a considerable sum for the rights, registered the trademark and continued importing the product while developing a business identity separate from that of the French manufacturer. When a competitor, Katzel, then began purchasing the product in France and selling it in the United States under the French trademark, Bourjois brought suit to enjoin Katzel from infringing on Bourjois' registered trademarks.⁸² The Second Circuit found no infringement under section 27 of the Trade-Mark Act of 1905,⁸³ since Katzel's goods were genuine in that they bore a genuine trademark.⁸⁴ Congress reacted to the perceived unfairness of the result in *Katzel*, not by amending the existing trademark laws, but rather by amending the Tariff Act.⁸⁵

lowing the Commission's determination in this case to stand could be viewed as an alteration of that interpretation. I, therefore, have decided to disapprove the Commission's determination.

78. *Vivitar Corp. v. United States*, 761 F.2d 1552 (Fed. Cir. 1985), *aff'g* 593 F. Supp. 420 (Ct. Int'l Trade 1984), *cert. denied*, 474 U.S. 1055 (1986).

79. *Coalition to Preserve the Integrity of American Trademarks v. United States*, 790 F.2d 903 (D.C. Cir. 1986), *rev'd* 598 F. Supp. 844 (D.D.C. 1984), *aff'd in part and rev'd in part sub nom. K Mart Corp. v. Cartier, Inc.*, 108 S. Ct. 1811 (1988).

80. 275 F. 539 (2d Cir. 1921), *rev'd.*, 260 U.S. 689 (1923).

81. Bourjois called the product "Poudre Java," whereas the product was called "Poudre de Riz de Java" before Bourjois purchased the rights. *Id.* at 540.

82. *Id.* at 540.

83. Section 27 of the Trade-Mark Act of 1905 was later reenacted as § 42 of the Lanham Act of 1946. See *infra* note 198.

84. *Katzel*, 275 F. at 543.

85. Note, *supra* note 43, at 91. The Tariff Act coincidentally happened to be before Congress at the time that Congress was responding to *Katzel*. *COPIAT v. United States*, 790 F.2d 903, 909 (D.C. Cir. 1986).

That amendment, section 526 of the Tariff Act of 1922, made the importation of goods bearing the same trademark as a genuine U.S. trademark unlawful without the consent of the U.S. trademark owner.⁸⁶

There is very little legislative history to shed light on the congressional intent of section 526. The provision was introduced as a floor amendment to the Tariff Act of 1922, and the debate on the proposed amendment, which was limited to only ten minutes, was "hasty, confused, and ill-informed."⁸⁷ The records from the debates indicated that the Senators were confused both about the nature of the proposed legislation⁸⁸ and the details in *Katzel*.⁸⁹ The language originally set out did not specify goods "of foreign manufacture" or "owned by a citizen of, or by a corporation or association created or organized within, the United States."⁹⁰ These changes were added as a result of Senate floor discussions.⁹¹ The final exchange of the debate has proven to be an important source for the interpretation of the congressional intent behind section 526 and has since been viewed in several ways by the courts.⁹² In the final minutes, Senator Lenroot asked whether section 526 would protect a foreign manufacturer whose American agent registered the trademark in the United States from parallel importation.⁹³ Senator McCumber's response was that only registered trademarks owned by American domiciliaries would be protected.⁹⁴ Dissatisfied with the response, Senator Lenroot rephrased his question to ask if an international trademark registered in the United States by an American domiciled in the United States could be brought in without the written consent of the American agent.⁹⁵

86. See *supra* note 10.

87. Kersner & Stein, *supra* note 23, at 258.

88. 62 CONG. REC. 11,602 at 11,605 (daily ed. Aug. 19, 1922). Senator McCumber mistakenly thought that the original version of § 526 protected only registered trademarks that were owned by American domiciliaries.

89. *Id.* at 11,603. Senator Moses stated that "the whole subject matter involved in this amendment is now before the courts of the United States for determination."

90. *K Mart Corp. v. Cartier, Inc.*, 108 S. Ct. 1811, 1823 (1988).

91. 62 CONG. REC. at 11,604.

92. See *Vivitar Corp. v. United States*, 761 F.2d 1552 (Fed. Cir. 1984), *cert. denied*, 474 U.S. 1055 (1988). "Our review of the comments in the floor debate leads us to the conclusion that the debate is too unfocused and misinformed to serve as a definitive basis for interpretation of § 1526." *Id.* at 1563; *Olympus Corp. v. United States*, 792 F.2d 315, 319 (2d Cir. 1986), *cert. denied*, 108 S. Ct. 2033 (1988) (not discussing the legislative history at length, because it agreed with the *Vivitar* court that § 1526 was adopted primarily to overturn the Second Circuit decision in *Katzel*); *COPIAT v. United States*, 790 F.2d 903, 912 (D.C. Cir. 1986), *rev'd in part and aff'd in part*, 108 S. Ct. 1811 (1988) (inferring from the legislative history that "the lawmakers consciously drew the line at American companies and did not adopt distinctions among different categories of American companies").

93. 62 CONG. REC. at 11,605.

94. *Id.*

95. *Id.*

Time ran out, and Senator Lenroot's question was never answered.⁹⁶ The sparse legislative history does not directly answer whether Congress really meant what it said in the statute about barring the importation of goods with the same trademark as a genuine U.S. trademark or whether it enacted section 526 merely to overrule the Second Circuit's decision in *Katzel*.⁹⁷

The Supreme Court heard *Katzel* several months after the enactment of section 526. In reversing the Second Circuit decision, the Court focused on two factors: Bourjois' purchase of the trademark rights from the foreign manufacturer and the goodwill value of the trademark.⁹⁸ The Court thereby rejected the prevailing legal theory of universality, which controlled the Second Circuit's decision in *Katzel*⁹⁹ as well as previous infringement cases.¹⁰⁰ The theory of universality states that trademarks do not confer property interests or monopoly power over intrabrand competition; instead, they protect the public from being deceived by indicating the origin of the trademarked goods.¹⁰¹ Under this theory, since trademarks are universal and not territorial, there could be no infringement when goods enter another country where the trademark has been registered.¹⁰² Consequently, the only remedy that an American assignee of a trademark right could have against the foreign assignor was in breach of contract or unfair competition.¹⁰³ In *Katzel* the Supreme Court instead adopted the doctrine of territoriality.¹⁰⁴ Whereas the focus of protection under the universality theory was the consumer and the origin of the product, the focus of protection under the territoriality the-

96. *Id.*

97. Note, *supra* note 35, at 846.

98. *A. Bourjois & Co., Inc. v. Katzel*, 260 U.S. 689, 692 (1923).

99. *A. Bourjois & Co., Inc. v. Katzel*, 275 F. at 543 (2d Cir. 1921). The court stated: "Trademarks . . . are intended to show without any time limit the origin of the goods they mark, so that the owner and the public may be protected against the sale of one man's goods as the goods of another man. If the goods sold are the genuine goods covered by the trade-mark, the rights of the owner of the trade-mark are not infringed." *Id.*

100. *E.g.*, *Apollinaris Co. v. Scherer*, 27 F. 18 (C.C.S.D.N.Y. 1886) (where an American had purchased the exclusive right to import certain bottled water into the United States and the right to use the trademark, and a third party began importing the water, the court found that since the water was genuine and the public was not deceived, there was no infringement); *Fred Gretsck Mfg. v. Schoening*, 238 F. 780 (2d Cir. 1916) (where the court found no infringement of a U.S. trademark on violin strings that were registered by the exclusive agency for sale in the U.S. when a competitor brought the violin strings from Germany, noting that § 27 of the Trademark Act of 1905 was designed to protect the public from goods that were not genuine).

101. *K Mart Corp. v. Cartier, Inc.*, 108 S. Ct. 1811, 1822 (1988).

102. Note, *supra* note 43, at 107.

103. *Atwood, Import Restrictions on Trademarked Merchandise—The Role of the United States Bureau of Customs*, 59 TRADEMARK REP. 301, 303 (1969). Thus, it was not considered unlawful for third parties who sold lawfully marked goods to compete with the U.S. trademark holder. *Id.*

104. *Katzel*, 260 U.S. at 692 (stating that the monopoly of a trademark is no less complete than the monopoly of a patent).

ory is the trademark holder and the separate legal existence of the trademark as the source of origin of the goods in each country in which it is registered.¹⁰⁵ The theory of territoriality recognizes that the function of the trademark is to symbolize the domestic goodwill in the mark.¹⁰⁶

The cases that were heard shortly after the passage of section 526 of the Tariff Act of 1922 suggest that the application of section 526 was not limited to the *Katzel* fact pattern. When the question of whether Customs should exclude genuine goods bearing a U.S. registered trademark arose in *A. Bourjois & Co. v. Aldridge*,¹⁰⁷ the Court determined that unauthorized genuine goods did "copy or simulate" the U.S. registered trademark and could be excluded under section 27 of the Trade-Mark Act of 1905.¹⁰⁸ The Court's determination that unauthorized genuine goods can be excluded under the Trademark Act implies that section 526 also encompasses more than the situation in which a U.S. company purchases the trademark rights of a foreign company in the U.S.¹⁰⁹ In *Coty, Inc. v. Le Blume Import Co.*¹¹⁰ the Second Circuit looked at the plain language of section 526 and allowed Customs to withhold the entry of the gray market perfume.¹¹¹ Judge Learned Hand stated that had the Supreme Court reversed *Katzel* earlier, Congress would not have enacted section 526, adding that section 526(a) was only meant to supply the

105. Note, *supra* note 43, at 107-108.

106. Note, *supra* note 35, at 841. "[D]omestic trademarks are distinct from identical foreign trademarks if the product has become associated in the public's mind with the American assignee and not with the foreign manufacturer." Note, *Should "Greymarket" Trade be Illegal? "COPIAT" Fuels the Controversy*, 7 J.L. & COM. 163, 168 (1987).

107. 263 U.S. 675 (1923) (per curiam).

108. *Id.* at 676. In 1913, the plaintiff, A. Bourjois & Co., Inc. purchased from Wertheimer & Cie., a French company, its entire U.S. business in certain toilet powders and face tints, including the "sole and exclusive right to manufacture and sell" them in the U.S. *A. Bourjois & Co., Inc. v. Aldridge*, 292 F. 1013, 1013-14 (1922). In 1915, the plaintiff registered the two trademarks, POU-DRE MANON LESCAUT and BOUQUET MANON LESCAUT, while Wertheimer & Cie. continued to produce and sell a product that was identical to the U.S. product in France. A third party, Benhart Co., bought some of the powder in France with the intention of importing it into the United States. Bourjois brought this suit against Aldridge, the collector of Customs at the port of New York, for declining to exclude the French product. *Id.* at 1014. The two questions certified by the Second Circuit were:

(1) Is the sale in the United States of Wertheimer's Manon Lescaut powder an infringement of plaintiff's registered trade-marks?

(2) Is the collector, by section 27 of the Trade-Mark Law, required to exclude from entry genuine Manon Lescaut powder so as aforesaid made in France?

Id.

The Supreme Court answered both in the affirmative. 263 U.S. at 676.

109. Note, *supra* note 43, at 96-97. "*Aldridge* recognizes that exclusion of genuine goods should not be limited to technical and individual infringement determination made by some courts today." *Id.* at 97.

110. 292 F. 264 (S.D.N.Y. 1923), *aff'd*, 293 F. 344 (2d Cir. 1923).

111. *Coty* had moved to dismiss LeBlume's motion to compel *Coty* to withdraw its notice to Customs to keep the gray market perfume from entering the country. *Id.* at 265.

casus omissus that existed in section 27 of the Trade-Mark Act of 1905, and thus the business relationship between the foreign and domestic markholders was irrelevant under section 526.¹¹² In a third case, the Second Circuit did not permit an American tourist to import a car bearing the same trademark as that held by a U.S. registered trademark for her personal use. In *Sturges v. Clark D. Pease, Inc.*,¹¹³ the court stated that “[b]y the Tariff Act Congress adopted the policy of protecting the American owners of foreign trademarks by the most drastic means.”¹¹⁴ Thus, early case interpretations of section 526 indicate that the courts viewed the statute without the restrictions later imposed by Customs.

The Tariff Act of 1922 was repealed and reenacted as the Tariff Act of 1930 without any changes.¹¹⁵ Later, while Congress was in the process of holding hearings on the then proposed Lanham Trade-Mark Act of 1946, the United States Tariff Commission¹¹⁶ submitted to Congress a memorandum, which pointed out the current administrative practices as well as the relationship between section 526 of the Tariff Act of 1930 and section 27 of the Trade-Mark Act of 1905.¹¹⁷ Though Congress considered taking the provisions of section 526 out of the Tariff Act and putting them instead into the Trade-Mark Act, in the end, section 42 of the Lanham Act was simply a reenactment of section 27 of the Trade-Mark Act of 1905, and section 526 of the Tariff Act was left intact.¹¹⁸ Thus, Congress, aware of the existing conflict regarding the coverage of section 526, chose not to change section 526.¹¹⁹ Congress later considered amending section 526 when it was discussing the Customs Simplification Act of 1954. The proposed amendment¹²⁰ would have excluded from the pro-

112. *Id.* at 269. The *Osawa* court gave the following explanation of what Judge Learned Hand meant by *casus omissus*: “What Hand’s observation meant was only that the passage of § 526 would have been unnecessary and would not have occurred if the *Bourjois* Supreme Court decision had been rendered earlier, bringing such “genuine” goods within the coverage of § 27.” *Osawa & Co. v. B & H Photo*, 589 F. Supp. 1163, 1175 (S.D.N.Y. 1984).

113. 48 F.2d 1035 (2d Cir. 1931). The decision in this case was overturned in 1978 by the passage of § 526(d).

114. *Id.* at 1038. The court added, “However much we may differ with its policy, the wisdom of the legislation is for the lawmaking body, and we cannot say that the means adopted were unadapted to the end sought to be attained.” *Id.*

115. The Senate unsuccessfully attempted to amend § 526 by banning all imports of goods bearing a U.S. registered trademark by deleting the provision that requires the trademark owner’s consent to allow such imports. See generally, Kersner & Stein, *supra* note 23, at 259-60.

116. The United States Tariff Commission is now called the International Trade Commission. *COPIAT v. United States*, 790 F.2d 903, 914 (D.C. Cir. 1984).

117. *Id.*

118. Atwood, *supra* note 103, at 306. “From 1938 until 1946, all the reports accompanying the trademark bills which culminated in the Lanham Act stated that their purpose was to clarify the law and to remove laws relating to trademarks from such unlikely places as tariff acts.” *Id.*

119. *COPIAT*, 790 F.2d at 914.

120. H.R. 9476, 83d Cong., 2d Sess. 6 (1954). The proposed amendment stated, in relevant part:

tection of section 526 American trademark owners affiliated with owners of identical trademarks.¹²¹

Antitrust considerations regarding the anticompetitive effects of manufacturer-imposed intrabrand restrictions¹²² came into play in the 1950s. The Justice Department filed suit in 1957 against three perfume importers, charging them with unlawful monopolization under section 2 of the Sherman Act in *United States v. Guerlain, Inc.*¹²³ The importers had been assigned the perfume trademarks by the manufacturer, who continued to supply them the perfume. The U.S. licensees tried to bar the entry of the gray market perfume under section 526 of the Tariff Act.¹²⁴ The district court ruled in favor of the government, holding that the Tariff Act must be viewed in light of the antitrust laws¹²⁵ and that section 526 does not extend its protection to a registered U.S. trademark holder who is part of a single international business enterprise.¹²⁶ The court agreed with the Justice Department that there is a "related party" exception to section 526 and that a *per se* violation of the Sherman Act occurred whenever the U.S. trademark holder imposed restrictions on product distribution once the product had already been released into commerce.¹²⁷ The court found that the trademark was an important element in selling the perfumes and rejected the defendants' arguments about the free-ride the gray-market importers had on their advertising efforts, since the profitability of the gray market imports in itself was

SEC. 526. Merchandise Bearing American Trade-Mark.

(a) Unless written consent of the owner of a mark or name entitled to the protection of this section is produced at the time of making entry, it shall be unlawful to import into the United States any merchandise of foreign manufacture if such merchandise, or the label, sign, print, package, wrapper, or receptacle bears a name or mark which copies or simulates a mark registered in the Patent Office on the principal register . . . or under the name of any domestic manufacturer, or trader, or of any manufacturer or trader located in any foreign country which, by treaty, convention, or law affords similar privileges [sic] to citizens of the United States, provided that a copy of the certificate of registration of such mark or the name entitled to the above protection is filed with the Secretary of the Treasury, in accordance with regulations which the Secretary shall prescribe.

121. *COPIAT*, 790 F.2d at 915. The bill closely paralleled the provisions of the Customs regulation § 133.21(c). *Id.*

122. Intrabrand competition is among distributors of the product of a particular manufacturer, whereas interbrand competition is among the manufacturers of the same "generic" product. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 52 n.19 (1977).

123. 155 F. Supp. 77 (S.D.N.Y. 1957), *vacated and remanded*, 358 U.S. 915 (1958), *action dismissed*, 172 F. Supp. 107 (S.D.N.Y. 1959). The defendants were Guerlain, Inc., Parfums Corday, Inc., and Lanvin Parfums, Inc.

124. *Id.* at 79.

125. *Id.* at 83.

126. *Id.* at 91.

127. Hilliard, *supra* note 7, at 4-5. This was consistent with the view that prevailed in the 1960s and 1970s that manufacturer-imposed restrictions on distribution of products after their release into commerce was a *per se* Sherman Act violation. *Id.*

evidence of the anti-competitive impact.¹²⁸ The appeal went directly to the Supreme Court. However, at the request of the Solicitor General, who promised to encourage Congress to clarify the Tariff Act, the Court vacated the decision in *Guerlain* with prejudice to the government without hearing the case.¹²⁹

In the aftermath of *Guerlain*, in 1959 Congress considered the Celler Bill¹³⁰ that would have repealed section 526 altogether. After a debate over trademark property rights and the conflicting antitrust concerns, that proposal was also defeated in committee before hearings were even held.¹³¹ In 1969, an attempt to repeal section 526 while Congress was considering an amendment to the Lanham Trade-Mark Act of 1946 failed.¹³² Congress did, however, amend section 526 in 1978 when it created an exception in section 526(d)¹³³ for goods brought into this country by individuals for their personal use.¹³⁴ Senator Chafee's attempt in 1986 to amend section 526 of the Tariff Act to provide for the parallel importation of goods also failed.¹³⁵ The most recent effort to amend section 526 was proposed on February 2, 1989 and would provide for parallel importation under section 526 of the Tariff Act of 1930.¹³⁶ This proposed amendment, however, is countered by a Senate bill that would ban

128. *Guerlain*, 155 F. Supp. at 87, 89.

129. The Supreme Court vacated the decision with prejudice to the government, even though the district court had ruled in favor of the government. Atwood, *supra* note 103, at 306-307.

130. The Celler Bill, H.R. 7234, 86th Cong., 1st Sess. (1959), in relevant part:

SEC. 2. Section 45 of this Act (15 U.S.C. 1127) is amended by changing the period at the end of the sentence defining "counterfeit" to a comma and adding, "but it does not include a mark used by a foreign manufacturer or merchant to identify and distinguish his goods and registered to a person who is an agent, authorized distributor, or subsidiary of, or who is affiliated with or is controlled by, such foreign manufacturer or merchant. The term 'affiliated,' as employed herein and in section 42(b)(1), shall include, but not be limited to, an exclusive or a nonexclusive distribution contract and any arrangement whereby the person has a continuing contractual relationship or understanding, express or implied, with the foreign manufacturer or merchant with regard to the mark."

Sec. 3. Section 526 of the Tariff Act of 1930 (June 17, 1930, ch. 497, 46 Stat. 741; 19 U.S.C. 1526) is repealed.

131. *COPIAT v. United States*, 790 F.2d 903, 915 (D.C. Cir. 1986). For discussions that present contrasting views of the Celler Bill, see generally, Derenberg, *Current Trademark Problems in Foreign Travel and the Import Trade*, 49 TRADEMARK REP. 674 (1959) and Vandenburg, *The Problem of Importation of Genuinely Marked Goods is not a Trademark Problem*, 49 TRADEMARK REP. 707 (1959).

132. S. 3713, 90th Cong., 2d Sess. (1968).

133. 19 U.S.C. § 1526(d)(1) (1978). See *supra* note 10 for text of the statute.

134. One court found that this exemption further suggests that Congress' intent in passing § 526 was to exclude all genuine goods bearing the U.S. registered trademark without the domestic owner's authorization. *United States v. Eighty-Nine Bottles of Eau de Joy*, 797 F.2d 767, 771 (9th Cir. 1986).

135. S. 2614, 99th Cong., 2d Sess. (1986). For the text of the bill, see *supra* note 66.

136. H.R. 771, 101st Cong., 1st Sess. (1989). See also *supra* note 68.

parallel importations by amending the Lanham Act.¹³⁷

B. Customs Regulation 133.21

After the enactment of section 526 of the Tariff Act of 1922, the U.S. Customs Service, a part of the United States Treasury Department, was assigned the task of promulgating regulations for the administration and enforcement of the statute.¹³⁸ An examination of the Customs regulations regarding trademarks reveals that the Customs Service's policy has not been consistent over the years.¹³⁹ The Customs Regulations of 1923 did not specify what constituted a violation of section 526.¹⁴⁰ Thus, Customs was not carving out any exceptions to section 526's protection at that time. After the enactment of the Tariff Act of 1930, the Customs Regulation of 1931 likewise provided total protection against the importation of genuine goods bearing a U.S. trademark without the consent of the trademark owner.¹⁴¹

In 1936 the Customs Regulation began to change. The Customs Regulation of 1936, article 518, no longer referred to section 526 of the Tariff Act. Because the Customs Service attempted to respond to the language of section 27 of the Trade-Mark Act of 1905,¹⁴² article 518 refers to goods bearing trademarks that copy or simulate U.S. trademarks.¹⁴³ Moreover, article 518 exempted articles that bear foreign trademarks owned "by the same person, partnership, association, or corporation" as the registered U.S. trademark from the protection offered by section 27 of the Trade-Mark Act of 1905.¹⁴⁴ Congress considered article 518 in 1944 when it held hearings on legislation that would become

137. S. 626, 101st Cong., 1st Sess. (1989). At the time of the publication of this Note, this bill was still in committee. See also *supra* note 69.

138. See 19 U.S.C. § 1624 (1982) *supra* note 14.

139. Atwood, *supra* note 103, at 301.

140. *Vivitar Corp. v. United States*, 593 F. Supp. 420, 428 (Ct. Intl. Trade 1984) (discussing Articles 475-480 of the Customs Regulations of 1923).

141. *Vivitar Corp. v. United States*, 761 F.2d 1552, 1566 (Fed. Cir. 1985) (finding that the bar against genuinely trademarked goods in Article 518(a) of the Customs Regulation of 1931 appeared to be absolute).

142. *COPIAT v. United States*, 790 F.2d 903, 914 (D.C. Cir. 1986).

143. Customs Regulations of 1936, Art. 518 in relevant part: Prohibition of importation —

(a) Merchandise of foreign or domestic manufacture is prohibited importation when it bears a name or mark which copies or simulates a trade-mark or trade name entitled to the protection of the Trade-Mark Act of 1905 or the Trade Mark Act of 1920, unless such merchandise is imported by or for the account of, or with the written consent of, the owner of the protected trade-mark or trade name.

T.D. 48,537, 70 Treas. Dec. 336, 337 (1936).

144. *COPIAT*, 790 F.2d 903, 914 (stating that "it is doubtful that amended Article 518 even purported to interpret Section 526 as well as Section 27," but Customs did refer to § 526 in 1943 when it recodified its regulations).

the Lanham Trade-Mark Act of 1946.¹⁴⁵ In a memorandum it submitted to Congress, the United States Tariff Commission referred to article 518 as promulgating section 27 of the Trademark Act of 1905 rather than section 526 of the Tariff Act of 1930, even though “[s]ection 526 of the tariff act does apply to the merchandise of the trade-mark owner which bears his trade-mark if the merchandise was produced abroad and if the trade-mark owner is a citizen of the United States.”¹⁴⁶ Thus, it was an *informed* Congress that passed section 42 of the Lanham Act of 1946, leaving section 526 of the Tariff Act as it was.¹⁴⁷

In 1951, Frank Dow, then Commissioner of Customs, sent a letter to Senator Paul H. Douglas in which he stated that the Customs Service did not view section 526 as barring the importation of trademarked goods of the foreign subsidiary of an American trademark owner.¹⁴⁸ In 1953, the Customs Service promulgated new regulations under 19 C.F.R. § 11.14.¹⁴⁹ The amended regulation made no reference to section 526 as a statutory authority.¹⁵⁰ In addition, it no longer barred goods without the U.S. trademark owner’s consent if the foreign trademark was owned by a “related company” as defined by section 45 of the Lanham Act of 1946,¹⁵¹ which covers both licensees and commonly-owned companies.¹⁵² However, as it became known during the *Guerlain* litigation,¹⁵³ in practice, some U.S. trademark owners enjoyed more protection than others, depending on whether their trademarks were recorded before or after disclosure of affiliates became obligatory under the 1953 amended regulation.¹⁵⁴ The Customs Service responded to *Guerlain* in 1959 by withdrawing all reference to “related companies” from 19 C.F.R. § 11.14.¹⁵⁵ The new regulation removed the protection of section 526

145. *Id.*

146. *Hearings Before a Subcomm. of the Comm. on Patents on H.R. 82, United States Senate, 78th Cong., 2d Sess.* 87 (1944).

147. *COPIAT*, 790 F.2d at 914.

148. *Id.* at 914-15.

149. The 1953 amended version of 19 C.F.R. § 11.14(b) denied the protection of § 526 when the foreign and U.S. trademarks were owned by “a related company as defined in Section 45 of the Trade-Mark Act of 1946.” T.D. 53,399, 88 Treas. Dec. 376, 384 (1953).

150. *Id.* at 385; *COPIAT*, 790 F.2d at 915 (the D.C. Circuit stating that evidence suggested that Customs nevertheless continued to consider related companies as outside the protection of § 526).

151. Note, *supra* note 43, at 99 n.91. “The term ‘related company’ means any person who legitimately controls or is controlled by the registrant or applicant for registration in respect to the nature and quality of the goods or services in connection with which the mark is used.” 15 U.S.C. § 1127 (1982).

152. *Vivitar Corp. v. United States*, 761 F.2d 1552, 1566 (Fed. Cir. 1985).

153. *United States v. Guerlain, Inc.*, 155 F. Supp. 77 (S.D.N.Y. 1957). For discussion, see *supra* notes 123-129 and accompanying text.

154. *Vivitar*, 761 F.2d at 1566.

155. *Atwood*, *supra* note 103, at 310 (notwithstanding, Customs continued to exclude goods from the protection of § 526).

only from U.S. trademark owners who owned rights abroad and thus were considered the "same entity," thereby reverting to its 1936 exception.¹⁵⁶ There could be no uniform enforcement of this new regulation, however, since disclosure was only required for principal/agent relationships.¹⁵⁷ Thus, under the 1959 regulation, Customs denied the protection of section 526 when the domestic and foreign trademark were owned by the same person, partnership, association, or corporation,¹⁵⁸ even though it had deleted the "related company" exception.

Customs again promulgated new regulations in 1972. It is the 1972 regulation, section 133.21(c)¹⁵⁹ that has been challenged in the courts and that was at issue in the *K Mart* case. Section 133.21(c) has been viewed as implementing the Customs Service's perception of antitrust law¹⁶⁰ as a reaction to *Guerlain*.¹⁶¹ It contains the "same entity" limitations of the 1953 and 1959 regulations; in addition, it excludes from the protection of section 526 all owners of a U.S. trademark with common ownership or parent/subsidiary relationships with foreign companies, as well as licensed foreign manufacturers.¹⁶² Customs has been criticized for its reasoning in this regulation for several reasons: first of all, the rationale of the district court opinion in *Guerlain* was repudiated by the Supreme Court,¹⁶³ secondly, Customs lacks the expertise and authority to interpret antitrust law,¹⁶⁴ and finally, antitrust theory has changed a great deal since the late 1950s when *Guerlain* was heard.¹⁶⁵ For example, while the Supreme Court supported the Customs regulation when it found *per se* violations of the Sherman Act arising from manufacturer-imposed intrabrand restrictions on the distribution of products after the products had been released into commerce,¹⁶⁶ that opinion was later

156. *Vivitar*, 761 F.2d at 1567 (the "same entity" requirement was satisfied by parent/subsidiary relationships).

157. *Id.*

158. Note, *supra* note 43, at 100 n.97.

159. See *supra* note 15 and accompanying text.

160. *COPIAT v. United States*, 790 F.2d 903, 915 (D.C. Cir. 1986) (noting that the notice in the Federal Register that accompanied the 1972 regulation, 37 Fed. Reg. 20,677 (1972), did not explain the Customs Service's reasoning behind this regulation).

161. *Id.* at 916.

162. Customs requires disclosure of all names of those affected by section 133.21(c). 19 C.F.R. § 133.2 (1972).

163. *United States v. Guerlain, Inc.*, 358 U.S. 915 (1958).

164. Note, *supra* note 35, at 848. Only the Justice Department and the Federal Trade Commission have been given antitrust enforcement powers. *Id.* at 848 n.67. The *Osawa* court called § 133.21(c) "unsound both as antitrust policy and as trademark law." *Osawa & Co. v. B & H Photo*, 589 F. Supp. 1163, 1178 (S.D.N.Y. 1984).

165. *COPIAT v. United States*, 790 F.2d 903, 916 (D.C. Cir. 1986).

166. *Olympus Corp. v. United States*, 792 F.2d 315, 319-20 (2d Cir. 1986) (citing *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 379 (1967)).

overruled.¹⁶⁷ The Court instead found that restrictions on intrabrand distribution may in fact promote interbrand competition.¹⁶⁸ Thus, the Supreme Court had cast doubt on the appropriateness of regulations that rest on antitrust considerations.¹⁶⁹

Even Customs has sought a clarification of the protection provided to trademark holders under section 526. In 1983 Customs along with the Department of Justice filed an amicus brief in *Bell & Howell: Mamiya Co. v. Masel Supply Co.*,¹⁷⁰ which dealt with the question of the importation of gray market cameras brought as a violation of section 42 of the Lanham Act. Curiously, the brief urged the court to give section 526 "the normal meaning of the statutory language,"¹⁷¹ which suggests full protection to the trademark owner, without any exceptions.

The history of the Customs regulations enforcing section 526 indicates that Congress has known that Customs has made exceptions to the protection of section 526 by refusing to bar the entry of certain gray market goods. When Congress, aware of administrative policy, acts on certain legislation in certain ways without upsetting the administrative policy, it is said that Congress has acquiesced to that policy.¹⁷² The policy of the Supreme Court in reviewing an agency's interpretation of a statute is to examine the statutory language along with the design and purpose of the statute.¹⁷³ With an agency regulation the first question to be decided is whether the agency's interpretation is a permissible construction of the statute,¹⁷⁴ and, if there is no conflict with the purpose of the statute, the Court will defer to that agency's interpretation.¹⁷⁵

167. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 58 (1977).

168. *Id.* at 54. The Court noted that interbrand competition "provides a significant check on the exploitation of intrabrand market power because of the ability of consumers to substitute a different brand of the same product." *Id.* at 52 n.19.

169. *Olympus*, 792 F.2d at 320.

170. 719 F.2d 42 (2d Cir. 1983).

171. *Vivitar*, 761 F.2d at 1568. *See also*, *COPIAT*, 790 F.2d at 916.

172. "When an agency's interpretation and application of a particular statute are known to Congress, and Congress either amends the statute without affecting the administrative practice or refuses to act at all, the administrative interpretation of a law is presumed to be correct and consistent with Congressional intent." *COPIAT v. United States*, 598 F. Supp. 844, 852 (D.D.C. 1984) (citing *Haig v. Agee*, 453 U.S. 280, 297-98 (1981)).

173. *K Mart Corp. v. Cartier, Inc.*, 108 S. Ct. 1811, 1817 (1988) (citing *Bethesda Hosp. Assn. v. Bowen*, 485 U.S. 399 (1988)).

174. *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984). When deciding whether an interpretation is a permissible construction of a statute, the Court is faced with the question of whether Congress has directly spoken to that issue. If the answer is yes, then the agency must give effect to that expressed intent. If Congress has not directly addressed a particular question in issue, the Court must decide if the agency's interpretation is a reasonable construction of the statute. *Id.* at 842-43.

175. *Id.* at 844 (legislative regulations are given controlling weight unless arbitrary, capricious, or manifestly contrary to the statute).

The scant legislative history of section 526 has led to conflicting interpretations of the legislative intent in enacting section 526 of the Tariff Act of 1930. Courts have been faced with deciding on the validity of the interpretation that the Customs Service's regulation section 133.21(c) gives to section 526(a). In 1984 the owner of the VIVITAR trademark brought suit in the Court of International Trade¹⁷⁶ challenging section 133.21(c) *per se*. In *Vivitar Corp. v. United States*,¹⁷⁷ the Vivitar Corporation sought a declaratory judgment that would have the Customs Service exclude imports bearing the VIVITAR mark. The trademark owner was a California corporation that had granted a license to a foreign manufacturer. The goods manufactured in foreign countries were marketed abroad by wholly owned subsidiaries of the California corporation, but the subsidiaries had no authority to import the products into the United States.¹⁷⁸ The Vivitar Corporation argued that the independent dealers who were importing Vivitar products and selling them at lower prices were getting a free-ride on its legitimate business expenses. This free-ride would, in time, ruin the reputation and sales value of the VIVITAR trademark.¹⁷⁹ The Court of International Trade found that the Customs regulation was both consistent over time and a reasonable interpretation of section 526. The court concluded that section 526 was only passed to overturn the Second Circuit decision in *Katzel*, and that, therefore, the court did not believe that section 526 was meant to deal with the problem of free-riding on a trademark holder's goodwill, reputation and advertising. Moreover, the court added that international commerce had been

176. The Court of International Trade held that it had exclusive jurisdiction over the *Vivitar* claim. The court based its holding alternatively on 28 U.S.C. § 1581(i)(3) and/or (4). *Vivitar*, 760 F.2d at 1560.

28 U.S.C. § 1581 (i) (1986) states:

(i) In addition to the jurisdiction conferred upon the Court of International Trade by subsections (a)-(h) of this section and subject to the exception set forth in subsection (j) of this section, the Court of International Trade shall have exclusive jurisdiction of any civil action commenced against the United States, its agencies, or its officers, that arises out of any law of the United States providing for—

- (1) revenue from imports or tonnage;
- (2) tariffs, duties, fees or other taxes on the importation of merchandise for reasons other than the raising of revenue;
- (3) embargoes or other quantitative restrictions on the importation of merchandise for reasons other than the protection of the public health or safety; or
- (4) administration and enforcement with respect to the matters referred to in paragraphs (1)-(3) of this subsection and subsections (a)-(h) of this section.

The question of jurisdiction was raised in *K Mart*. The Supreme Court rejected the reasoning of the *Vivitar* court. *See infra* note 223.

177. 593 F. Supp. 420 (Ct. Intl. Trade 1984), *aff'd*, 761 F.2d 1552 (Fed. Cir. 1985), *cert. denied*, 474 U.S. 1055 (1986).

178. *Vivitar*, 761 F.2d at 1556.

179. *Id.* *Vivitar* justified its higher prices because it has legitimate business expenses that the discount houses that sell gray market goods do not have, e.g., advertising and warranty costs. *Id.*

substantially relying on the Customs regulation.¹⁸⁰

The Federal Circuit affirmed the Court of International Trade's holding that the Customs regulation was "a reasonable exercise of administratively initiated enforcement"¹⁸¹ and that "Customs is not required to exclude all grey market goods *sua sponte*."¹⁸² The Federal Circuit rejected, however, the Court of International Trade's views that section 526 was passed merely to overturn *Katzel*,¹⁸³ that the regulation had been consistent over the years, and that Congress had implied its consent of the regulation.¹⁸⁴ Instead, the court concluded that a trademark owner's recourse against parallel importation could be found in the courts, and the courts, in their discretion, could impose an injunction against the entry of particular gray market goods.¹⁸⁵

A similar suit, *Olympus Corp. v. United States*,¹⁸⁶ began in New York. The American Association of Exporters and Importers undertook to eliminate the exemption under section 133.21(c)(2) regarding parent/subsidiary relationships. Before turning to the courts for relief, the Olympus Corporation unsuccessfully lobbied to get Customs to abolish the related companies exception to section 526.¹⁸⁷ Customs and the Treasury Department "declined to change this practice by a mere regulatory change."¹⁸⁸ Consequently, the Olympus Corporation, which owns its U.S. trademark rights and an exclusive distributorship and is the wholly owned subsidiary of a Japanese corporation that manufactures cameras, lenses, flash units and filters, sought to enjoin the importation into the United States of Olympus products manufactured abroad without the written consent of the New York corporation. The K-Mart Corporation and 47th Street Photo, Inc. intervened as defendants because of their interest in gray market Olympus products. The district court found that section 133.21 was not contrary to section 526. Though the Second

180. *Vivitar*, 593 F. Supp. at 436.

181. *Vivitar*, 761 F.2d at 1571.

182. *Id.* at 1569.

183. *Id.* at 1565.

184. *Id.* at 1568.

185. *Id.* at 1569. The Federal Circuit remarked that the Customs regulation does not control on the question of whether gray market goods should be excluded. A trademark owner is free to pursue private remedies under § 526(c). *Id.* The remedies provided by § 526 are seizure and forfeiture of the merchandise (§ 526(b)) or an injunction and damages (§ 526(c)).

186. 627 F. Supp. 911 (E.D.N.Y. 1985).

187. Comment, *Customs—The Gray Market—The Latest Word: Olympus Corporation v. United States*, 792 F.2d 315 (2d Cir. 1986), 11 SUFFOLK TRANSNAT'L L.J. 209, 210 n.9 (1987). The vice president in charge of product importation of Olympus was also the chairman of the American Association of Exporters and Importers, which lobbied to have § 133.21(c)(2) eliminated. *Olympus Corp. v. United States*, 792 F.2d 315, 317 (2d Cir. 1986).

188. *Olympus*, 792 F.2d at 317 (quoting the letter from John M. Walker, Jr., Assistant Secretary of the Treasury, to Senator Paul S. Sarbanes).

Circuit found the regulation of “questionable wisdom,”¹⁸⁹ it upheld the district court’s decision on the grounds that congressional acquiescence to the regulation made the Customs Service’s longstanding interpretation of section 526 legitimate.¹⁹⁰ The court in *Olympus* agreed with the *Vivitar* court that section 526 was passed to overturn *Katzel*,¹⁹¹ but it disagreed with the latter in that it found that the regulations have been sufficiently consistent. The *Olympus* court noted that there would be administrative difficulties in excluding gray market goods at the borders and suggested that it would be a good policy for Congress to change the regulations.¹⁹² The court pointed out that, despite the validity of the Customs regulations, trademark owners could pursue a private right of action under section 526(c).¹⁹³ Judge Winter dissented, stating that section 526 was not only easy enough to enforce, but that it was not clear what relevant policy the Customs regulation was meant to implement. He denounced the theory that Congress’ longstanding acquiescence carries with it little weight where the Customs Service itself has been confused about the regulation’s purpose and validity.¹⁹⁴ Finally, a third suit was brought by an association of owners of registered U.S. trademarks, the Coalition to Preserve the Integrity of American Trademarks (“COPIAT”). In *Coalition To Preserve the Integrity of American Trademarks v. United States* (“COPIAT”),¹⁹⁵ the organization, COPIAT, challenged the validity of Customs regulation section 133.21(c) as had been done in *Vivitar* and *Olympus*. The district court in *COPIAT* found the regulation valid as a sufficiently reasonable interpretation of the statute, basing its view on the legislative history and on congressional acquiescence of Customs’ longstanding interpretation of the statute.¹⁹⁶ The District of Columbia Court of Appeals reversed the district court’s judgment, finding Customs regulation section 133.21(c) invalid,¹⁹⁷

189. *Id.* at 320.

190. *Id.* at 321.

191. *Id.* at 319.

192. *Id.* at 320-21.

193. *Id.* at 320. For the text of § 526(c), see *supra* note 10. In a recent private action under § 526(c) in which the plaintiff was a U.S. wholly owned subsidiary of a Japanese firm the court refused to grant an exclusion order. The court, while agreeing that the Customs regulations do not define the full scope of protection provided by § 526(a), gave § 526(a) the same interpretation as was given by the Customs Service. *Yamaha Corp. of Am. v. ABC Int’l Traders Corp.*, 703 F. Supp. 1398, 1403 (C.D. Ca. 1988).

194. *Olympus*, 792 F.2d at 322 (Judge Winter agreeing with the D.C. Circuit’s opinion in *COPIAT* regarding the congressional intent behind the enactment of § 526). See generally *infra* notes 196-197 and accompanying text.

195. 598 F. Supp. 844 (D.D.C. 1984). The K-Mart Corporation and 47th Street Photo, Inc. intervened as defendants, as they had done in *Olympus*.

196. Note, *supra* note 5, at 1046.

197. *COPIAT v. United States*, 790 F.2d 903, 918 (D.C. Cir. 1986).

thereby creating a split in the circuits in disagreement with the *Vivitar* and *Olympus* decisions. It was *COPIAT* that reached the Supreme Court as *K Mart Corp. v. Cartier, Inc.*

Recently, the D.C. Circuit heard a case in which Customs regulation 133.21(c)(2) was again challenged, but this time as an interpretation of section 42 of the Lanham Act, which prohibits the importation of goods that copy or simulate goods that bear a U.S. registered trademark.¹⁹⁸ The plaintiff in *Lever Bros. v. United States*,¹⁹⁹ a U.S. corporation that manufactures Shield soap and Sunlight dishwasher detergent, has an affiliated corporation in the United Kingdom.²⁰⁰ While the wrapping used on the products is similar, the ingredients differ for the British and U.S. markets.²⁰¹ Third parties have been importing the U.K. products into the United States without the authorization of Lever Brothers.²⁰² Customs has been allowing the gray market goods into the United States under the section 133.21(c) exception to section 42 of the Lanham Act, regarding as irrelevant the differences in the U.K. and the U.S. products.²⁰³ Lever Brothers contended, however, that though the goods bear the same genuine trademark, the differences in physical content result in the foreign products copying or simulating the domestic trade-

198. Section 42 of the Lanham Act of 1946 has been codified as 15 U.S.C. § 1124 (1978). It reads:

Importation of goods bearing infringing marks or names forbidden

Except as provided in subsection (d) of section 1526 of Title 19, no article of imported merchandise which shall copy or simulate the name of the [sic] any domestic manufacture, or manufacturer, or trader, or of any manufacturer or trader located in any foreign country which, by treaty, convention, or law affords similar privileges to citizens of the United States, or which shall copy or simulate a trademark registered in accordance with the provisions of this chapter or shall bear a name or mark calculated to induce the public to believe that the article is manufactured in the United States, or that it is manufactured in any foreign country or locality other than the country or locality in which it is in fact manufactured, shall be admitted to entry at any customhouse of the United States; and, in order to aid the officers of the customs in enforcing this prohibition, any domestic manufacturer or trader, and any foreign manufacturer or trader, who is entitled under the provisions of a treaty, convention, declaration, or agreement between the United States and any foreign country to the advantages afforded by law to citizens of the United States in respect to trade-marks and commercial names, may require his name and residence, and the name of the locality in which his goods are manufactured, and a copy of the certificate of registration of his trademark, issued in accordance with the provisions of this chapter, to be recorded in books which shall be kept for this purpose in the Department of the Treasury, under such regulations as the Secretary of the Treasury shall prescribe, and may furnish to the Department facsimiles of his name, the name of the locality in which his goods are manufactured, or of his registered trademark, and thereupon the Secretary of the Treasury shall cause one or more copies of the same to be transmitted to each collector or other proper officer of customs.

199. 877 F.2d 101 (D.C. Cir. 1989).

200. *Id.* at 102.

201. *Id.* at 103.

202. *Id.*

203. *Id.* at 104.

mark.²⁰⁴ Though the D.C. Circuit remanded the case so that the district court could do a detailed examination of the legislative history and administrative practice, the court clearly indicated that, in its opinion, the district court would hold section 133.21(c)(2) invalid in regard to section 42 of the Lanham Act.²⁰⁵ The significance of *Lever Brothers* in light of the *K Mart* decision is that it indicates that *K Mart* neither resolved the controversy regarding the Customs regulation nor presented any kind of definitive statement regarding the gray market.

III. K MART CORP. V. CARTIER, INC.

A. Procedural History

The suit that eventually made its way to the Supreme Court as *K Mart v. Cartier* was brought by American manufacturers and distributors of registered trademarked products who were suing either individually or by representation by the organization to which they belonged, the Coalition to Preserve the Integrity of American Trademarks (COPIAT). The trademarked goods included such items as perfumes, cosmetics, watches, tires, crystal, cameras and other photographic equipment, binoculars and electronic goods. The plaintiffs, U.S. trademark owners, were seeking an order directing the Customs Service to exclude from entry into the United States certain gray market goods that were manufactured by the foreign subsidiaries or licensees of the U.S. trademark owners and brought into this country by unrelated third parties without the authorization of the U.S. trademark owners.²⁰⁶

The third party importers and dealers were allegedly obtaining a free-ride on the goodwill and advertising that the trademark owner had established in the United States and then underselling the authorized U.S. dealers by as much as thirty percent.²⁰⁷ The plaintiffs claimed that they were entitled to have the gray market goods excluded under both section 42 of the Lanham Act of 1946 and section 526(a) of the Tariff Act of 1930.²⁰⁸ The defendants in the case were the United States of America, the Secretary of the Treasury, and the Commissioner of the United States Customs Service. Two retailers that sell such gray market

204. *Id.* at 103.

205. *Id.* at 111. The court said, "We think the natural, virtually inevitable reading of § 42 is that it bars foreign goods bearing a trademark identical to a valid U.S. trademark but physically different, regardless of the trademark's genuine character abroad or affiliation between the producing firms." *Id.*

206. COPIAT v. United States, 598 F. Supp. 844, 846 (D.D.C. 1984).

207. *Id.* at 850.

208. *Id.* at 846.

goods intervened as defendants, the K-Mart Corporation, which operates more than 2000 discount department stores, and 47th Street Photo, Inc., which sells camera, video and other electronic equipment.²⁰⁹

After deciding that it had subject matter jurisdiction in this case,²¹⁰ the district court dismissed the claim under section 42 of the Lanham Act for failing to state a claim upon which relief can be granted, since the trademarks in this case were not "counterfeit or spurious."²¹¹ After an examination of the history of section 526 of the Tariff Act and of the Customs regulation, section 133.21(c), the court remarked that Congress, by not altering the Customs Service's interpretation of the statute, approved of the regulation.²¹² Furthermore, the court found Customs' interpretation of the statute "long-standing and consistent," and as such it deserved to be given "considerable weight."²¹³ Finally, the court concluded that the regulation was a sufficiently reasonable interpretation of section 526, since the statute was meant merely to cover the *Katzel* situation, that is to say, a situation in which a foreign manufacturer sells its trademark rights to an American and then tries to market its goods in the United States through channels other than the American purchaser.²¹⁴

Though the Court of Appeals for the District of Columbia agreed with the district court about the jurisdictional issue, it disagreed with the district court's holding on the merits of the case, finding the Customs regulation a violation of section 526.²¹⁵ The court did not decide whether the regulation violated section 42 of the Lanham Act because it had already held that section 133.21(c) was invalid since it could not be squared with section 526 of the Tariff Act.²¹⁶ After a detailed analysis of the legislative and judicial history of section 526, the court concluded that the congressional intent in section 526 was clear; there are no exceptions to the statute's coverage,²¹⁷ since the statute was written to protect all trademarks "owned by a citizen of . . . the United States, and regis-

209. Several importers and distributors of gray market goods presented amicus briefs. *Id.* at 846-47.

210. Whereas the Court of International Trade in *Vivitar* held that it had exclusive jurisdiction over claims arising under § 526 of the Tariff Act under 28 U.S.C. § 1581(a), the *COPIAT* court held that it had general federal question jurisdiction under 28 U.S.C. § 1331 and specific jurisdiction under 28 U.S.C. § 1338(a) of actions relating to trademarks. *COPIAT*, 598 F. Supp. at 847.

211. *Id.* at 848 (absent the *Katzel* situation, § 42 only applies to "merchandise bearing counterfeit or spurious trademark that 'copy or simulate' genuine trademarks").

212. *Id.* at 852.

213. *Id.*

214. *Id.*

215. *COPIAT v. United States*, 790 F.2d 903, 905 (D.C. Cir. 1986).

216. *Id.* at 907.

217. *Id.* at 908.

tered in the Patent and Trademark Office by a person domiciled in the United States . . . unless written consent of the owner of such trademark is produced at the time of making entry."²¹⁸ The appellate court added that the theory of congressional acquiescence accepted by the district court was too tenuous.²¹⁹ The Court of Appeals for the District of Columbia not only dismissed the district court's view that the regulation was a sufficiently reasonable interpretation of section 526, but it also rejected the Federal Circuit's reasoning in *Vivitar* that the regulations could be upheld "as a reasonable exercise of administratively initiated enforcement"²²⁰ since Customs had never really justified the regulation as an exercise of enforcement discretion.²²¹ However, despite the D.C. Circuit's holding that Customs regulation section 133.21(c) was invalid, the court would only grant declaratory relief, since the injunctive relief sought was "not an order compelling the Customs Service to exclude specific goods, but rather a broad decree that would entail continuing supervision by the courts."²²²

B. *The Supreme Court*

Justice Kennedy wrote the relatively short, straightforward opinion for the Court. Justice Brennan, who would have held all three subsections of the regulation valid, wrote a detailed opinion concurring in part and dissenting in part, offering a different rationale for finding section 133.21(c)(1) and (2) valid. Justice Scalia, on the other hand, who also wrote a detailed opinion concurring in part and dissenting in part, would have found all three subsections of the regulation invalid. The Justices based their interpretations on the language of the regulation vis-à-vis section 526 and on their different views of the legislative history. Significantly, the Court did not address the related issue of whether the regulations are inconsistent with section 42 of the Lanham Act, which prohibits the importation of goods that bear marks that "copy or simulate" U.S. trademarks.

1. The Decision

In *K Mart Corp. v. Cartier, Inc.*,²²³ the opinion of the Supreme

218. 19 U.S.C. § 1526(a) (1975).

219. *COPIAT*, 790 F.2d at 917 (the unsuccessful attempts to modify § 526 suggest that Congress rejected a narrow view of the scope of § 526).

220. *Vivitar Corp. v. United States*, 761 F.2d 1552, 1571 (Fed. Cir. 1985). See also *supra* notes 181-182 and accompanying discussion.

221. *COPIAT*, 790 F.2d at 918.

222. *Id.*

223. 108 S. Ct. 1811 (1988). The jurisdiction issue was heard separately in *K Mart Corp. v.*

Court²²⁴ began with a presentation of three cases in which the gray market problem may arise.²²⁵ The first case, referred to by the Court as the prototypical case, resembled the facts in *Katzel*. It involves a domestic firm that purchases the trademark rights from a foreign firm in order to register the trademark and sell the goods in the United States. Intradbrand competition might arise if either the foreign manufacturer could, notwithstanding the fact that it had sold the exclusive rights to an American firm to market the goods in the United States, import the goods into this country or if third parties could purchase the foreign firm's goods abroad and then import them into the United States. The resulting parallel importation could jeopardize the domestic trademark owner's investment.²²⁶ All of the Justices agreed that under the case 1 scenario section 526 bars the importation of gray market goods.²²⁷

The second case involves a domestic firm that registers the trademark in the United States for goods that an affiliated manufacturer has manufactured in a foreign country.²²⁸ The Court presented three variations of this case. In what the Court called case 2a, the foreign firm wishes to control the sale and distribution of its goods in the United States. The foreign firm, therefore, incorporates a subsidiary in the United States, which, in turn, registers a trademark identical to its foreign parent's trademark under its own name in the United States. Parallel importation occurs when third parties, or even the affiliate itself, imports the registered trademarked goods into the country.²²⁹ In case 2b, an American firm establishes a subsidiary corporation abroad for the

Cartier, Inc., 108 S. Ct. 950 (1988). The Court held that the Court of International Trade did not have exclusive jurisdiction over this case. The only petitioner to contest the jurisdiction, 47th Street Photo, Inc., offered two theories. First, 28 U.S.C. § 1581 (i) (3) (*see supra* note 176 for text) gives the Court of International Trade exclusive jurisdiction over suits involving embargoes. The Supreme Court rejected this argument, since § 526 does not impose an embargo on gray market goods because it is the U.S. trademark holder who requests, at its option, the help of the Customs Service in restricting the entry of certain goods. Justice Scalia, in his dissenting opinion, disagreed with the Court about whether § 526 imposes an embargo.

The second theory presented by 47th Street Photo, Inc. was that the Court of International Trade has jurisdiction over cases that contest the administrative "denial of a protest" challenging the Custom's excluding of goods from entry. The Court rejected this theory as well, since the action involves a challenge to the entry rather than to the exclusion of certain gray market goods. The Court found that this case did not involve a "protest" and thus did not fall under the exclusive jurisdiction of the Court of International Trade.

224. Justice Kennedy was joined with respect to Parts I and II-A by Rehnquist, C.J., and White, Blackmun, O'Connor, and Scalia, JJ., with respect to Part II-B by White, J., and with respect to Part II-C by Rehnquist, C.J., and Blackmun, O'Connor, and Scalia, JJ. *K Mart Corp. v. Cartier, Inc.*, 108 S. Ct. at 1814.

225. *Id.* at 1814-15.

226. *Id.*

227. *Id.* at 1818.

228. *Id.* at 1815.

229. *Id.*

manufacture of goods, and in case 2c the American firm establishes an unincorporated manufacturing division abroad. In both cases 2b and 2c the foreign division manufactures the goods for distribution in the United States. The parallel importation occurs when the goods are sold abroad to a third party, who then imports the goods into the United States.²³⁰

The third case is one in which the domestic holder of the registered U.S. trademark authorizes an independent foreign manufacturer to use the trademark. Generally the foreign manufacturer is given the exclusive right to use the trademark and to distribute the goods abroad on condition that the goods are not imported into the United States. Again, parallel importation occurs when either the foreign manufacturer reneges on its promise not to import the goods into the United States or when a third party purchases the goods abroad and then imports them into the United States.²³¹

The Court then analyzed the Customs regulation in question, section 133.21(c), which creates exceptions for certain categories of goods to exclude them from the overall protection of section 526(a) of the Tariff Act of 1930. The Court separated the three subparts of the regulation into two categories, the common-control exception to section 526 and the authorized-use exception. The Court upheld the validity of the common-control exception incorporated in section 133.21(c)(1)-(2), which does not restrict imported goods if either the foreign and U.S. trademark is owned by the same person or entity or if the foreign and domestic trademark owners are parent/subsidiary companies or otherwise subject to common control or ownership.²³² The Court held invalid the authorized-use exception in section 133.21(c)(3), which allows the importation of goods that bear a registered trademark under the authorization of the U.S. trademark holder.²³³

In reaching its conclusion, the Court followed the standard by which it determines whether a regulation is a valid interpretation of a statute. The Court first looked at the language and design of the statute to determine if any ambiguities exist. The Court found two phrases in section 526 sufficiently ambiguous. The Court noted that the first term, "owned by," is unclear in that a trademark can be owned by more than one entity, such as a parent and a subsidiary of the same company. The Court also found the words, "of foreign manufacture" ambiguous in that they could mean either "in a foreign country," "by a foreign company,"

230. *Id.*

231. *Id.*

232. *Id.* at 1817.

233. *Id.*

or "in a foreign country by a foreign company."²³⁴

Since the Court found the language of section 526(a) ambiguous with respect to the issues addressed by the Customs regulation, the Court examined the agency's definition of the ambiguous terms and found that they were not in conflict with the statute and thus represented a reasonable construction of the statute. For that reason the Court found section 133.21(c)(1) and (2) valid.²³⁵ On the other hand, since the ambiguous language of the statute does not pertain to the authorized-use exception where there is no common ownership involved, the Court held that the statute protects trademark owners who have authorized foreign manufacturers to use the trademark; therefore, section 133.21(c)(3) is invalid.²³⁶ Because the invalidation of this subsection would not impair the functioning of the statute, and because there is no indication that the regulation would not have been passed if it were not for the inclusion of this subsection, the Court severed section 133.21(c)(3) from the rest of the regulation.²³⁷

2. Justice Brennan's Opinion²³⁸

Though Justice Brennan agreed with the holding that the common control exceptions, section 133.21(c)(1) and (2), were valid, his reasoning was different. In analyzing the language of section 526, he found a protectionist "flavor" indicating that Congress had meant to protect only domestic interests. Specifically, the statute requires that the trademark be registered in the U.S. Patent and Trademark Office, that the trademark holder be domiciled in the United States, and that the manufacturer be organized within the United States.²³⁹ As Justice Brennan analyzed the legislative history of section 526(a), he concluded that if Congress had any intent at all regarding the statute, it was to exclude foreign manufacturers from its protection.²⁴⁰ Justice Brennan arrived at this conclusion by distinguishing cases 1 and 2. The victim of the gray market importation in case 1, who has purchased the rights to register the trademark and sell the goods in the United States, has a large invest-

234. *Id.* at 1818.

235. *Id.* (when a statute is imprecise, the enforcing agency can choose any reasonable interpretation of the statute).

236. *Id.*

237. *Id.* at 1819.

238. *Id.* (Brennan, J., concurring in part and dissenting in part). Justice Brennan was joined by Marshall and Stevens, JJ. Justice White joined as to Part IV.

239. *Id.* at 1820 (protecting only domestic interests was characteristic of the times).

240. *Id.* at 1826. Moreover, much of the limiting language of § 526 would be pointless if a foreign manufacturer could insulate itself from competition from the sale of gray market goods by incorporating a subsidiary in the United States to register its trademark. *Id.* at 1820-21.

ment at stake with no control over the importation of gray market goods. On the other hand, the case 2 victim, who has a common ownership or parent/subsidiary relationship with the foreign company, has a number of options available, such as only importing directly to the affiliate, imposing restrictions against resale as a condition on its sales abroad, or curtailing sales abroad all together.²⁴¹

In addition, Justice Brennan noted that two of the three current limitations²⁴² to the statute were added after the original draft, namely "of foreign manufacture" and "owned by a citizen of, or by a corporation or association created or organized within, the United States." Justice Brennan was of the opinion that the legislative history indicates that section 526 was enacted to overrule *Katzel*.²⁴³ While conceding that the circuit court's reading of the legislative history was plausible, Justice Brennan rejected it. In Justice Brennan's view, had Congress passed section 526 to reject the prevailing universality theory which stated that trademarks did not confer property rights over the trademarked goods, Congress not only would have acknowledged such a rejection, but it would have referred the matter to a committee to be studied.²⁴⁴

Justice Brennan then considered the Customs regulation, concluding that the agency has "always denied complete exclusionary protection to an American trademark registrant when it knew the importer to be a subsidiary or parent of the foreign user of the trademark."²⁴⁵ Since the Supreme Court does not lightly overturn longstanding administrative regulations, and since the business community has relied on this administrative interpretation of the statute, Justice Brennan agreed that the common control exceptions are valid.²⁴⁶

Justice Brennan then focused on the authorized-use exception, section 133.21(c)(3), which excludes from the protection of section 526 U.S. trademarked goods when the trademark owner has given licenses to foreign manufacturers to use their trademarks. Justice Brennan found am-

241. *Id.* at 1823.

242. The three limitations in § 526 of the Tariff Act of 1930 are: 1) when the product is "of foreign manufacture;" 2) when it bears a trademark "owned by" either a U.S. citizen or "a corporation . . . created or organized within the United States;" and 3) when "a person domiciled in the United States" has registered the trademark. *Id.* at 1820.

243. *Id.* at 1823.

244. *Id.* at 1826 (before effecting a radical change in prevailing legal doctrine, Congress refers the matter to a committee with expertise in the area).

245. *Id.* at 1828 (citing Atwood, *supra* note 103, at 307). Before 1953, however, Customs was not specifically eliciting information whether a parent/subsidiary relationship existed between the U.S. and foreign trademark holders. Atwood, *supra* note 103, at 307.

246. *Id.* at 1828 (a large domestic retail industry developed in reliance on Customs interpretation of § 526).

biguity in the statute with regard to the authorized-use of a trademark, though he admitted that the ambiguity is not immediately apparent. According to Justice Brennan, the law was not clear regarding the transferring of trademark rights until after the passage of the Lanham Act of 1946. Therefore, Congress, when enacting section 526(a), did not address the case 3, authorized-use situation. In determining whether section 133.21(c)(3) represents a permissible construction of the ambiguous terms of the statute, Justice Brennan compared the case 1 victim, who has purchased the rights from a foreign company to register a trademark, to the case 3 victim, who has authorized a foreign company to use its trademark. Whereas the case 1 victim has no control over the importation of gray market goods, the case 3 victim has recourse, in that he can either revoke or deny licenses. In sum, Justice Brennan would uphold the entire regulation.²⁴⁷

3. Justice Scalia's Opinion²⁴⁸

In Justice Scalia's view, section 133.21(c)(1)(2) & (3) is in conflict with the clear language of section 526(a) of the Tariff Act. First considering the term, "owned by," Justice Scalia agreed that though the term is ambiguous when applied to domestic subsidiaries of foreign corporations (case 2a), he saw "owned by" as unambiguous as applied to cases 2b, where the goods are manufactured abroad by the domestic trademark owner's subsidiary, and 2c, where the goods are manufactured abroad by the trademark holder. Moreover, Justice Scalia found nothing ambiguous about the term "merchandise of foreign manufacture," which in common usage simply means goods manufactured abroad. Justice Scalia further noted that the Court's interpretation of "of foreign manufacture" may exclude even some case 1 victims from the protection of the statute, since it is possible for a foreign trademark owner to license one American firm to use its trademark in the United States and license other American firms to use its trademark in foreign countries. In this situation it is conceivable that other American firms could import the trademarked goods, since the goods would not be "of foreign manufacture." In addition, Justice Scalia pointed out that the Customs Service itself interpreted "of foreign manufacture" to mean manufactured abroad.²⁴⁹

247. *Id.* at 1830.

248. *Id.* at 1831 (Scalia, J., concurring in part and dissenting in part). Justice Scalia was joined by the Chief Justice and by Blackmun and O'Connor, JJ.

249. *Id.* at 1831-32. Another difficulty that Justice Scalia found with the majority's opinion is that although the Customs Service is informed of the country of origin of imported goods, there is no regulation requiring the registration of the nationality of the manufacturer. Justice Scalia saw the Court's holding as not only placing a burden on the Customs Service to devise a system whereby it

Justice Scalia agreed with the Court that there is no ambiguity in the statute vis-à-vis case 3. He disagreed with Justice Brennan's reasoning that, as Justice Scalia put it, "if the enacting Congress had foreseen modern circumstances, it *would* have adopted such an exception, since otherwise the effect of the law would extend beyond its originally contemplated purpose."²⁵⁰ According to Justice Scalia, each Congress has the opportunity to change laws when circumstances have changed since their enactment. Justice Scalia saw the power of the Court being exercised only 1) when it is clear that the circumstances that have changed were not envisioned by the enacting Congress and 2) when the changed circumstances cause the statute to exceed its original purpose. Justice Scalia did not see either condition met in this case. As for the first condition, Justice Scalia pointed to a number of cases, including *Katzel*, which indicated that Congress was familiar with the assignment of trademarks in different regions of the country, thereby suggesting that Congress chose not to create an exception when it enacted section 526(a). Secondly, Justice Scalia did not agree with Justice Brennan that the equities are different in cases 1 and 3. Justice Scalia did not believe that the case 3 victim, who has authorized a foreign company to use its trademark, has any less investment at stake or any more control over the importation of gray market goods than does the case 1 victim, who has purchased its trademark rights, especially since it is usually third parties who are doing the damage.²⁵¹ In sum, Justice Scalia believed that section 526(a) goes beyond the facts of *Katzel*.²⁵²

IV. ANALYSIS

The title of the case, *K Mart Corp. v. Cartier, Inc.*, itself, naming a large American retailer and a well-known, high priced brand-name, indicates how big the financial interests involved in the gray market issue are. The opinion in *K Mart* reflects certain deficiencies in the clarity of the law regarding the importation of gray market goods. The real issue is whether gray market goods *should* be allowed into the country. Instead, the question presented to the Court was whether Customs *may* let them in, and that question was in the very small context of the Tariff Act. The decision can only be disappointing for both proponents and opponents of

becomes informed of the manufacturer's nationality, but also as conflicting with "mutually accepted understandings" with trading partners, who might not appreciate a regulation that treats American manufactured goods on American soil better than American manufactured goods in foreign countries.

250. *Id.* at 1834.

251. *Id.* at 1836.

252. *Id.*

the gray market, since each had fingers crossed that the Supreme Court would officialize the policy preferred by their side. *K Mart* demonstrates that the legal issue of whether the Customs regulation is valid and the policy issue of whether the gray market importation of goods should be banned cannot be resolved by the same forum. Moreover, recent litigation has shown that the validity of the same Customs regulation is still being challenged vis-à-vis section 42 of the Lanham Act.²⁵³

To arrive at its conclusion, the Court focused on two phrases in the statute and asked whether they were ambiguous and whether the Customs Service's interpretation was consistent with the meaning of the statute. This approach, along with the Court's depiction of the several common cases in which gray market importation results, differs considerably from the approaches used by the lower courts. To begin with, this approach lends itself to the type of diffusion of opinions that was seen in *K Mart*. The fact that the Justices did not agree on the various combinations of results available under this approach in itself both points to weaknesses of the approach and reflects the magnitude of the issue. From the lower courts up through the Supreme Court, a number of learned judges and Justices have been faced with the issue of the validity of the Customs regulation that excludes certain gray market goods from the protection of section 526(a) of the Tariff Act. What reached the Supreme Court was a conflict between a particular statute and regulations that interpret it. The statute in question is itself the center of controversy with the Customs regulation masking the real issue of whether allowing the importation of gray market goods is a sound policy or not. However, for the moment at least, the Supreme Court has the last word on the validity of section 133.21(c) with respect to the Tariff Act,²⁵⁴ thus the last word on which gray market goods may legally enter the country.

A. *Inherent Difficulties of a Linguistic Analysis*

The approach taken by the Supreme Court in *K Mart* in itself demonstrates that the judiciary is not the proper vehicle for a final determination of the gray market problem. The Court was limited to the discrete issues presented to it. The real conflict behind the *COPIAT* litigation involved the questions of whether gray market goods should be banned

253. *Lever Bros. v. United States*, 877 F.2d 101 (D.C. Cir. 1989). *Lever Bros.* raises issues about material differences between goods made for the domestic market and gray market goods that may eventually need to be resolved by the Supreme Court. For a discussion of *Lever Bros.*, see *supra* notes 199-205 and accompanying text.

254. As the D.C. Circuit's opinion in *Lever Bros.* demonstrates, since Customs has used the same regulation to interpret § 42 of the Lanham Act, the controversy over § 133.21(c) is not over.

from U.S. markets and how far a U.S. registered trademark protects its holder. The Court, however, was not faced with answering the real gray market questions, but rather was faced with analyzing an administrative agency's interpretation of a statute.

Predictably, the Court scrupulously analyzed the language of both section 526(a) and the Customs regulation. The majority opinion laid the foundation for the subsequent analysis of the meaning of the language of the statute first by depicting certain general contexts in which parallel importation of goods may occur, and then by categorizing the regulation itself into common-usage and authorized-use exceptions.²⁵⁵ Justice Kennedy in essence made only a passing reference to the legislative history of the statute and the Customs regulation by explaining in a footnote that the threshold question is essentially whether the language of the statute is ambiguous and whether the regulation is a permissible construction of the statute.²⁵⁶

The more interesting analyses in *K Mart* can be found in the tension between Justices Brennan and Scalia in their opposite views of the interpretation of section 526(a) and its legislative history. Justice Brennan's focus on the protectionist slant of the statute²⁵⁷ appeared to be a reasonable explanation of the congressional intent in passing section 526 until Justice Scalia pointed out that assignments of goodwill and trademark rights to those doing business in different areas of the country was a common enough practice before the passage of section 526(a).²⁵⁸ In two different parts of his opinion Justice Brennan presented the trademark owner with certain facile options to eliminate or alleviate the flow of parallel importations of their goods.²⁵⁹ Justice Scalia capsulized his contrary view of the extent of the problem when, toward the end of his opinion, he stated, "It is not the affiliates who are doing the damage but third parties."²⁶⁰

With the framework of the Court's analysis set on the language of the statute, Justice Brennan's study turned toward the legislative history

255. *K Mart*, 108 S. Ct. at 1816.

256. *Id.* at 1815.

257. *Id.* at 1820.

258. *Id.* at 1835. Unrelated businesses in different territories could own and use an identical trademark even before 1920, which meant that a trademark owner doing business in one territory could assign the business, goodwill and rights to the trademark in a different territory. Justice Scalia supported these assertions with case cites from that era. *Id.*

259. *Id.* at 1823, 1830. Even Justice Brennan's options are plagued with the insertion, "if legal" and do not take into account that the trademark holder must abide by the laws of the other countries he is dealing with, and thus the options may not in fact be available.

260. *Id.* at 1836 (since third parties are responsible for "the bulk of the gray market," affiliated trademark holders are also deserving of protection under § 526).

of section 526. When, however, his historical analysis reached the 1950s, Justice Brennan simply glossed over that era in a parenthetical stating "for reasons not relevant here."²⁶¹ Yet, the events of the *Guerlain* litigation were significant in molding the Customs' current interpretation of section 526(a).²⁶² In fact, none of the Supreme Court opinions in *K Mart* ever mentioned the *Guerlain* case, which, according to the lower courts and to many scholars, was the very basis of the Customs regulation in question in *K Mart*, section 133.21(c).²⁶³ The fact that in 1959 the Supreme Court deferred to the Solicitor General's request to vacate the holding in *Guerlain* in order to get a clarification on the controversy from Congress is in itself certainly an important topic to consider in analyzing the history of the statute and the Customs regulation. Customs has been accused of basing its current interpretation of section 526(a) on its view of outdated antitrust considerations regarding intrabrand competition.²⁶⁴ The circuit court in *COPIAT* addressed its concern about the influence of *Guerlain* on the current regulation,²⁶⁵ yet none of the Supreme Court opinions responded to that concern.

In contrast to both the majority's and Justice Brennan's opinions, Justice Scalia did not see ambiguity in the words of the statute.²⁶⁶ Justice Scalia pointed out the deficiencies in the majority's rigid application of its rule of ambiguous language by showing how the majority's holding may inadvertently exclude some case 1 victims, who, as U.S. firms, have purchased trademark and goodwill rights from a foreign firm.²⁶⁷ He also had difficulty accepting the Court's view that the statute's protection extends only to the case 1 type victims when other victims of the gray market have at least as much of an investment and as little control over the influx of gray market goods as the case 1 victim.²⁶⁸ Justice Scalia concluded that since the gray market problem is generally attributable to

261. *K Mart*, 108 S. Ct. at 1820.

262. *COPIAT v. United States*, 790 F.2d 903, 916 (D.C. Cir. 1986) (citing Letter from Treasury Secretary Donald T. Regan to Senator Dennis De Concini, December 23, 1983 (the regulations are based on the *Guerlain* case)).

263. See *supra* note 163 and accompanying discussion.

264. *COPIAT*, 790 F.2d at 916. The Court held that intrabrand competition may in fact have procompetitive effects. *Continental T.V., Inc. v. GTE Sylvania*, 433 U.S. 36, 54 (1977). See *supra* notes 160-168 and accompanying discussion.

265. *COPIAT*, 790 F.2d at 915-16. *Guerlain* was also addressed by the *Vivitar* and *Olympus* courts. *Vivitar Corp. v. United States*, 761 F.2d 1552, 1566-67 (Fed. Cir. 1984); *Olympus Corp. v. United States*, 792 F.2d 315, 319 (2d Cir. 1986).

266. *K Mart*, 108 S. Ct. at 1831-32. "[I]t is impossible to conclude that a trademark owned by a United States corporation and applied abroad either by the corporation or its foreign subsidiary is 'owned by' anyone other than a United States corporation." *Id.* at 1831. "The phrase 'of foreign manufacture' is a common usage, well understood to mean 'manufactured abroad.'" *Id.* at 1832.

267. *Id.* at 1836.

268. *Id.* (the equities involved in case 1 and case 3 do not differ significantly since the vulnerabil-

third parties, it is not reasonable to conclude that some trademark owners have a greater need for the protection of section 526.²⁶⁹

The opinions of Justices Brennan and Scalia are important in that they shed more light on what the Court considered in arriving at the holding. The Court's focus on the linguistic details of section 526 and the Customs regulation that interprets it led to a holding that neither accepted nor rejected the gray market as a U.S. policy. The Supreme Court's analysis of the construction of the statute and regulation was destined to be inadequate as a final statement on the gray market problem. This inadequacy becomes particularly striking in light of more recent challenges to the Customs regulation section 133.21(c) through section 42 of the Lanham Act. If *Lever Brothers*²⁷⁰ eventually reaches the Supreme Court, a linguistic approach as was seen in *K Mart* might very well result in certain subsections of the Customs regulation being valid for the Tariff Act and invalid for the Lanham Act, or vice versa.

B. Policy Considerations

Whether one is for or against the gray market, the Supreme Court decision does not settle the matter in a final, satisfying way. The task of deciding on a gray market policy is not an easy one. Congress as a whole has generally avoided the issue over the course of the years. The recent effort by the Reagan Administration to come up with a single gray market policy likewise ended with the committee offering a list of options rather than a single concrete policy recommendation.²⁷¹ The difficulty with formulating a definite policy statement is that, whichever side of the gray market is adopted, somebody will be adversely affected, be it the trademark holder, the gray market importers and dealers, or even the consumer. The benefit to be derived from a clarification on the law regarding the gray market importation of goods is that, though some people will be initially hurt, a definite policy will provide predictability around which business plans could be made. Under the status quo, more damage is done by the lack of clarity since trademark holders are permitted to bring suits against gray market importers under various legal theories²⁷² to have a court determine on a case-by-case basis if the trademark

ity to gray market imports, the investment in goodwill, and the lack of direct control over the harm is the same in both cases).

269. *Id.*

270. *Lever Bros. v. United States*, 877 F.2d 101 (D.C. Cir. 1989).

271. See *supra* note 62 and accompanying discussion.

272. The legal theories under which a plaintiff can file a trademark infringement suit are § 42 of the Lanham Act, unfair competition under § 337 of the Tariff Act, and trademark infringement under state law. Bender and Gerber, *supra* note 13, at 15, col. 3. Additional theories include unjust

holders have a right to some sort of relief, be it exclusion or damages. This results in a waste of judicial resources and great expense for the trademark holders who pursue such lawsuits as well as for the gray market importers and retailers who must defend them.

The *K Mart* decision has shown that the Supreme Court is not the proper vehicle for a gray market policy decision. Only Congress is in a position to take into account the larger scheme, which includes not only the Tariff Act and the Lanham Act, but also economic and antitrust considerations, all within an international context.

First, Congress must consider the legal issue of how broadly to extend the coverage of the Tariff Act and the Lanham Act together, both in terms of the protection for the trademark holder and the protection the trademark offers the consumer. An attempt to amend either the Tariff Act or the Lanham Act singularly, without taking the other into consideration, may lead to the same confusion that currently exists regarding the breadth of protection and would leave a door open for another legal theory under which to pursue a gray market lawsuit.²⁷³

The purpose of trademark laws, to protect the investment in goodwill and reputation of the U.S. registered trademark holder, necessarily enters into a policy determination of whether the extent of this protection outweighs any economic benefits of the gray market business. Since trademark laws are also designed to protect the consumer, there are a number of factual considerations to take into account. One consideration, for example, is whether the goods involved are identical and have the same origin. Congress may make a distinction between goods that are of truly identical quality and those that look alike but are materially different, i.e., that have a shorter life span, different taste, etc., or that contain different warranties which can confuse the consumer. However, such distinctions may be difficult for Customs to implement, since they would require assessments about "material" differences at the border.²⁷⁴

enrichment, third party beneficiary, and interference with contractual relations. Coggio, Gordon & Coruzzi, *The History and Present Status of Gray Goods*, 75 TRADEMARK REP. 433, 487-93 (1986).

273. Of the two bills that are pending at the time of this Note, the House bill would allow the importation of gray market goods by amending the Tariff Act. H.R. 771, 101st Cong., 1st Sess. (1989). If this bill passes, trademark holders will still have a private right of action to pursue remedies under various legal theories, as they do now. The Senate bill, on the other hand, aims to place a total ban on the importation of gray market goods. S. 626, 101st Cong., 1st Sess. (1989). If this bill passes, a clear gray market policy will be achieved, since all gray market goods will be stopped at the border. The result would be an end to the ambiguity of both allowing gray goods to enter the country and then permitting litigation to sort out the rights of the particular parties. The Senate bill, though presented as an amendment to the Lanham Act, encompasses the entire gray market situation.

274. For example, Customs has referred to its interpretation of the Lanham Act as "an administrative necessity," since Customs would otherwise have to evaluate the amount of consumer confu-

Another consideration is whether a demarking or a labeling requirement such as Customs considered in its call for public solicitation in 1986²⁷⁵ would resolve the trademark confusion problem. Moreover, such factual considerations in a gray market decision must be balanced against economic concerns.

A gray market policy that protects certain parties over others will have economic consequences. There are pros and cons on both sides of the economic issue. Though the importation of gray market goods is closely tied to the fluctuating price of the dollar,²⁷⁶ an entire business has evolved around gray market imports. The economic justifications for the gray market have been that gray market goods represent savings of up to forty percent to the U.S. consumers.²⁷⁷ Congress will have to decide whether or not such competition among products within the same brand has a positive effect on the nation's economy. On the other side of the coin is the question whether permitting parallel importations would have the adverse effect of discouraging domestic trademark holders or distributors from investing in quality, research and development, and warranties or other consumer services. The argument is that the consumer could suffer in the long run if trademark owners cease to invest in continuing research and development to maintain high quality control. Like the legal issue of trademark protection, the issue of whether gray market importations are beneficial for the U.S. economy does not have an obvious answer and will require a careful balancing of interests.

There are international ramifications to the problem since the statute in question is found in the Tariff Act and involves goods coming in from foreign countries. Though the United States has unique domestic policy considerations that may not result in the same perception of parallel importation that other nations have, any gray market policy that the United States adopts will have an effect on the exports of another nation. A discussion of the gray market importation of goods cannot lose sight of the international context in which it plays a role. Most of our major trading partners have legalized the parallel importation of goods, and thus it has been argued that "[i]t would be entirely inappropriate for the U.S. Government to provide protection to foreign manufacturers whose own governments do not provide comparable protection for discrimina-

sion or loss of goodwill that might result from the importation of the goods. *Lever Bros. v. United States*, 877 F.2d 101, 110 (D.C. Cir. 1989).

275. See *supra* note 63 and accompanying discussion.

276. Bender & Gerber, *supra* note 13, at 15, col. 1. Though by the time *K Mart* was decided the dollar was low, the dollar may again rise substantially, some goods may be less affected by the fluctuations in the dollar, and the importation of some luxury goods flourishes despite the dollar. *Id.*

277. 132 Cong. Rec. S8741-42 (daily ed. June 26, 1986) (statement of Sen. Chafee).

tory pricing by American manufacturers."²⁷⁸

While an understanding of the international perspectives on parallel importation of goods is certainly desirable, foreign perspectives cannot be controlling since they do not necessarily reflect American concerns. The economic considerations of a U.S. gray market policy do not exactly mirror the economic viewpoints of our trading partners. The nations of the world have different points of departure in determining their gray market policies. For example, in the United States, the fluctuation in the U.S. dollar has played an important role in the gray market importation of goods into this country, and it has been argued that trademark owners are charging over-inflated prices in their American markets.²⁷⁹ The E.E.C. countries, on the other hand, have treaty commitments among themselves,²⁸⁰ which provide these nations with trade benefits that may offset any disadvantage imposed by parallel importation. In addition to the greater economic considerations, Congress may decide that the United States places a more important weight on trademark and consumer protection than do our trading partners. Thus, while keeping in mind the U.S. interface with the international community, Congress must, nonetheless, carve out a gray market policy best suited for U.S. interests which can be clearly understood by the other nations in the international community.

The changes that have occurred since the passage of the Tariff Act of 1930 have been significant enough to warrant a reassessment of section 526(a) in a context that includes other legislation that has an impact on the gray market. The courts, culminating with the Supreme Court, have offered various reasonings in support of or against the Customs Service's interpretation of the statute. However, the center of the controversy is section 526 of the Tariff Act, and that is what Congress should review. If, in fact, the gray market importation of goods is in the best interest of the United States, it should not be validated through the back-door approach of a Supreme Court linguistic study of the words of a statute that was enacted in 1930. The task is not an easy one. A large number of economic interests are at stake. Since the status quo, which lacks clarity in the U.S. gray market policy, also results in adverse effects for some

278. *Id.* at S742 (Senator Chafee arguing that the U.S. trademark laws are being exploited by foreign manufacturers who then charge the American public over-inflated prices for their goods).

279. *Id.*

280. The Treaty of Rome, which was signed in 1957, established the European Economic Community. The Treaty contains provisions that restrict competition within the E.E.C. Takamatsu, *supra* note 42, at 447.

parties, it is the policy itself that must be faced squarely, not just the words of the statute.

C. *Impact of the Decision*

Now that the Supreme Court has had the final word, or at least the most recent word, on the validity of section 133.21(c), the question becomes what impact the decision will have. The issues of U.S. policy regarding the importation of gray market goods and the extent of the protection afforded the U.S. trademark holder under section 526(a) have not been answered. The *K Mart* result, that gray market goods from firms that have been only authorized to use a U.S. registered trademark may no longer be brought across the U.S. borders, whereas gray market goods from firms with a "common control" may enter the country, seems almost arbitrary in terms of the larger gray market picture.

More important, the *K Mart* decision will influence the expansion of business arrangements in the international arena, since companies must now take the new Customs regulation into account when deciding whether to incorporate or to grant licenses to use a particular trademark abroad. For example, a U.S. company may decide only to license a foreign firm to use its trademark in order to insure control by having such goods stopped at the border, whereas had the Supreme Court found the entire regulation either valid or invalid, the same company may have chosen to incorporate a subsidiary.

The *K Mart* holding will not change the situation for a number of trademark owners or gray market importers, since a trademark owner's right to seek remedies other than exclusion at the border will remain the same.²⁸¹ The courts will still be faced with making case-by-case decisions. The trademark owner who has "common control" affiliations with foreign firms using the U.S. registered trademark will still have to be on the lookout for gray market freeloaders in order to find relief in the courts. The uncertainties that accompany litigation will remain the same for both the trademark holder and the gray market importer. The problem of unidentified third parties bringing in gray market goods will continue to burden the trademark owner's search for the source of the gray market importation.²⁸² The third parties who are importing the gray market goods will continue to run the risk of being haled into court.

281. Section 526(c) gives the trademark owner a private right of action. *See supra* note 10.

282. There are detective agencies that specialize in locating the third parties that are importing gray market goods. *See Gerber, Litigating the Copyright "Gray Market" Case, in GRAY MARKETS AND PARALLEL IMPORTATION* 269, 289 (Practising Law Institute ed. 1986).

The severing of section 133.21(c)(3) will clearly restrict the importation of gray market goods produced by manufacturers who are licensed to use the trademark in foreign countries. Customs will have to note which goods come from a licensed foreign manufacturer and bar the entry of those goods at the border. Confusion may arise where the same American trademark holder has licensed a firm in one country to use its mark and has a subsidiary in another country that is also using its mark. If third parties are attempting to bring in the gray market goods, Customs may have difficulty identifying the source in order to decide whether to bar the entry of the goods.

The Supreme Court decision did not address the Customs Service's discretion regarding section 42 of the Lanham Act of 1946. The suit originally brought in *COPIAT* alleged a violation of section 42 of the Lanham Act as well, but that claim was dismissed at the district court level and did not reach the Supreme Court.²⁸³ The exceptions created by Customs regulation section 133.21(c) also extend to section 42 of the Lanham Act.²⁸⁴ Consequently, trademark owners may still bring suit under section 42 under the theory that the gray market good, though bearing a valid trademark, is not identical to the U.S. trademarked product in quality. Recent litigation, however, strongly suggests that section 133.21(c) has not left the spotlight.²⁸⁵ Moreover, section 337, which addresses unfair practices in import trade, still remains another possibility for suit. In addition, infringement claims can still be brought under state law.²⁸⁶ In short, the legal alternatives and remedies that existed for trademark holders before *K Mart* have not changed.

All that the *K Mart* decision defines is what will be stopped at the border and what will not. Trademark owners, of course, would prefer to have the Customs Service police the arrival of goods to prohibit the entry of those goods which would interfere with their established reputations and businesses. Gray market importers approve of the Customs regulations that allow their goods unimpeded entry into the United States. However, allowing the entry of goods and then permitting litigation on the rights of the parties affected by that entry of goods is a waste of judicial time and effort. The only way to end the conflict and the waste is for Congress to make a policy determination once and for all.

283. *COPIAT v. United States*, 598 F. Supp. 844, 846 (D.D.C. 1984).

284. Staaf, *supra* note 1, at 204.

285. *Lever Bros. v. United States*, 877 F.2d 101 (D.C. Cir. 1989).

286. *Bender & Gerber*, *supra* note 13, at 15, col. 3.

D. Recommendation

Congress responded to the decision in *Katzel* with legislation to correct certain inequities. Congress should respond to *K Mart* with a deliberately thought-out policy determination that will clearly delineate guidelines for both trademark owners and importers of gray market goods. Banning the importation of gray market goods without the trademark owner's consent presents the best solution. A restriction on parallel importation would uphold the integrity of the U.S. registered trademark by fully protecting the property rights conferred on the trademark owner. In addition, the consumer would be best served both by the elimination of confusion that the gray market goods cause and by the continued quality and services provided by the trademark holder.

The problems of consumer confusion will continue to exist despite attempts to inform the public about gray market goods. Consumers are drawn to certain brand names over others because of advertising and services associated with the brand name. While labeling an item as a gray market good is a valid attempt to inform the public, any dissatisfaction with the gray market goodwill inevitably reflect negatively on the trademark itself and result in lower sales.

Related to consumer confusion is the problem of free-riding. Part of the large discrepancy between the prices charged by the authorized seller and the gray market seller is due to the fact that not only does the gray market seller not have the expenses of advertising, consumer education, and warranties of the authorized dealer, the gray market seller has a market only because of the recognized labels and goodwill established by the trademark owner. This situation is particularly exploitative since more frequently it is third parties unrelated to the business agreement that are profiting from the goodwill developed by the trademark owner. Allowing this unfair arrangement to continue can only discourage trademark holders from making the kinds of investments in maintaining a superior product and in advertisements that have attracted the consumers to their brands. Backing off from such investments can only harm the consumer in the long run.

While it is true that trademark holders are profiting from both the sales of their goods abroad and the inflated prices for the American market, as long as a healthy competition exists among different brands in the same markets, the consumers can make clear choices based on quality and price without the confusion that intrabrand sales present.

Therefore, of the two bills that are currently pending in Congress,²⁸⁷ the bill introduced by Senator Hatch as an amendment to the Lanham Act²⁸⁸ provides the better solution to the gray market problem. The amendment addresses the larger gray market context by placing a total ban on such imports, thereby clearly defining trademark rights and closing all ambiguous loopholes through which later litigation could be pursued. The House bill, introduced by Representative Chandler, on the other hand, merely addresses the narrower issue of the extent of protection provided by section 526, leaving open legal theories under which the trademark owner can still seek legal remedies. In sum, Senator Hatch's proposed amendment to the Lanham Act to ban all parallel importation provides the needed gray market policy statement and a solution to the gray market controversy.

V. CONCLUSION

The detailed linguistic study of section 526 of the Tariff Act that resulted in the majority opinion in *K Mart Corp. v. Cartier, Inc.* has little relation to the broader problem of the parallel importation of goods. The judicial system has attempted to resolve the problem by facing the interpretation that the challenged Customs regulation has given the purpose of section 526 of the Tariff Act. The result was a variety of approaches presented by the lower courts and finally a decision by the Supreme Court. Significantly, it took one group of five Justices to validate part of the regulation and five different Justices to invalidate the other part of the regulation. The case history not only reflects the complexity of the gray market issue, it also illustrates how inadequate the judicial system is as a forum to resolve essentially larger policy issues.

Though the law is settled, since the Supreme Court has settled it, there is little satisfaction with this anxiously awaited opinion, which merely defined which goods will be stopped at the border and which will not. Strong feelings run on both sides of the gray market issue. However, the Court's job is limited to the interpretation of existing statutes and regulations. There is a larger scheme to be considered that so far Congress has been reluctant to touch. Consequently, policy is being made through interpretative decisions. The American public deserves a policy statement, and that can only come from Congress. A total ban on gray market importations is the best solution.

287. S. 626, 101st Cong., 1st Sess. (1989).

288. H.R. 771, 101st Cong., 1st Sess. (1989).

